ANKARA YILDIRIM BEYAZIT UNIVERSITY
INSTITUTE OF SOCIAL SCIENCES
DEPARTMENT OF BANKING AND FINANCE

# THE ROLE OF ISLAMIC FINANCE IN REDUCTION OF FINANCIAL EXCLUSION IN ETHIOPIA

**MASTER THESIS**

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# PLAGIARISM

I hereby declare that all information in this thesis has been obtained and presented in accordance with academic rules and ethical conduct. I also declare that, as required by these rules and conduct, I have fully cited and referenced all material and results that are not original to this work; otherwise I accept all legal responsibilities.

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ABSTRACT

THE ROLE OF ISLAMIC FINANCE IN REDUCTION OF FINANCIAL EXCLUSION IN ETHIOPIA

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This research investigates the role of Islamic finance in combating financial exclusion in Ethiopia. It intends to assess the extent and the nature of religious driven financial exclusion of Ethiopian Muslims and the level of their participation in the existing interest free window banking system introduced to the sector recently. In order to collect data for the research, the researcher employed mixed approaches such as questionnaires and semi-structured interviews. The questionnaire was distributed to 321 respondents in Addis Ababa while the semi-structured interview was conducted with selected high-ranking bank officers. Findings show that, 94.4%, 87.2% and 69.2% of the respondents did not have access to credit, micro finance and insurance respectively. Additionally, 62.9% of respondents reported to have never used home financing such as condominium housing program. Religion was found to be the main factor for not accessing conventional financial services. Further, the research also found that 67.9% of respondents did not access interest free banking window products and services offered by conventional banks. This finding potentially implies the failure of the newly introduced interest free window in enhancing the inclusion of Ethiopian Muslims in the

financial system. The absence of full-fledged Sharia compliant financial institution in Ethiopia considerably contributed to the exclusion of Ethiopian Muslims in the country's economy. It is, therefore, an overdue task for Ethiopian government to accommodate the interest of its Muslim population in the financial system. This includes, but not limited to, the establishment of full-fledged interest free financial institutions, including interest free bank, insurance and microfinance institutions.

*Keywords*: Religious driven financial exclusion, Islamic finance, interest free window banking and full-fledged interest free finance.

# ÖZET

# ETİYOPYA'DAKİ FİNANSAL DIŞLANMANIN AZALTILMASINA İSLAMİ FİNANSIN ROLÜ

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Bu çalışmanın amacı, Etiyopya'daki finansal dışlanmayla mücadelede İslami finansın rolünü araştırmaktır. Bu doğrultuda çalışmada, Etiyopyalı Müslümanların dini esaslı finansal dışlanmasının kapsamı ve niteliği incelenmiş ve mevcut faizsiz bankacılık pencere sistemlerine katılım düzeyleri değerlendirilmiştir. Araştırma sürecinde veri toplamak için, anket ve yarı yapılandırılmış mülakatı içeren karma yöntem kullanılmıştır. Anketler, Etiyopya Addis Ababa'da yer alan 321 katılımcıya dağıtılırken, yarı yapılandırılmış mülakatlar ise yüksek rütbeli banka memurlarıyla yapılmıştır. Elde edilen bulgular, ankete katılanların sırasıyla %94.4, %87.2 ve %69.2'sinin kredi, mikro finans ve sigortaya erişimi olmadığını göstermektedir. Ek olarak, ankete katılanların %62.9'u toplu konut gibi ev finans programını hiç kullanmamış olduğunu belirtmiş ve din faktörü konvansiyonel finansal hizmetlere erişmemesi için ana faktör olarak ortaya çıkmıştır. Ayrıca, araştırmaya katılanların % 67.9'unun konvansiyonel bankaların sunduğu faizsiz bankacılık penceresi ürünlerine ve hizmetlerine erişmedikleri tespit edilmiştir. Bu bulgu potansiyel olarak yeni tanıtılan faizsiz pencerenin Etiyopyalı Müslümanları finansal sisteme dahil etmediğini ve başarısızlığa

uğradığı anlamına gelmektedir. Etiyopya'da tam teşekküllü Şeriat uyumlu bir finans kuruluşunun bulunmaması, Etiyopyalı Müslümanların ülke ekonomisine dahil edilememesinin nedenini oluşturmaktadır. Bu nedenle, Etiyopya hükümetinin Müslüman nüfusun finansal sisteme olan ilgisini uyandırmasının gecikmiş bir görev olduğu ifade edilebilir. Ek olarak bunlarla sınırlı olmamak üzere; faizsiz banka, sigorta ve mikrofinans kuruluşları da dahil olmak üzere tam teşekküllü faizsiz finansal kurumların kurulması da gerekmektedir.

*Anahtar Kelimeler*: Dini esaslı finansal dışlanma, İslami finans, faizsiz bankacılık penceresi, tam teşekküllü faizsiz finans.

DEDICATION

This thesis is dedicated to my Father Mohammed Hailu and My Mother Fentaye Tesema.

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| | |
|---|---|
| AAOFIFI | Accounting and Auditing Organization for Islamic Financial Institutions |
| AFI | Alliance for Financial Inclusion |
| CTI | Center for Technology Innovation |
| DBE | Development Bank of Ethiopia |
| EIASC | Ethiopian Islamic Affairs Supreme Council |
| FDIP | Financial and Digital Inclusion Project |
| GCC | Gulf Cooperation Council |
| GDP | Gross Domestic Product |
| GIFR | Global Islamic Finance Report |
| GDP | Gross Domestic Product |
| IFB | Interest Free Banking |
| IFSB | Islamic Financial Service Board |
| IIBI | Institute of Islamic Banking and Insurance |
| IMFIs | Islamic Microfinance Institutions |
| KMO | Kaiser-Meyer- Olkin |
| MINA | Middle East and North Africa |
| NA | Not Available |
| NBE | National Bank of Ethiopia |
| OECD | Organization for Economic Co-operation and Development |
| OIC | Organization of Islamic Cooperation |
| PBUH | Peace Be Upon Him |
| PCA | Principal Component Analysis |
| PLS | Profit and Loss Sharing |
| SPSS | Statistical Package for Social Sciences |
| UAE | United Arab Emirates |
| UFA | Universal Financial Access |
| UK | United Kingdom |
| US | Untied State |

# 1 INTRODUCTION

## 1.1 Research Background

Financial inclusion is directly related with economic growth (Sahay et al., 2015; Claessens, 2006). Making finance accessible for all is one of the key drivers of economic development and growth. Development economists give attention for financial inclusion and it is also one of the focus areas to create inclusive financial system (Mohieldin et al., 2011).

According to Global Findex database 2014, 2 billion adults are financially excluded and 350 million or 17% of them are from Sub-Saharan Africa countries (Demirgüç-Kunt et al., 2015). In 2013, the World Bank group president Jim Young Kim announced Universal Financial Access in 2020 vision (UFA 2020). This vision has given priority for 25 countries where 73% of their population are not accessing finance or financially excluded. Ethiopia is one of the countries included in UFA2020 (World Bank, 2016).

According to The World Factbook, in 2016, Ethiopian total population estimated to 100.2 million, of which 35% to 40% are Muslims. Ethiopia is the third in Africa and tenth in the world by numbers of Muslim population with more than 34 million Muslims. The main source of the country's economy is agriculture and 80% of the populations live in rural area.

The first modern bank in Ethiopia, Abyssinia Bank, was established in 1906 (Mauri, 2003). After the fall of Dergue Regime in 1991, Ethiopia shifted towards free market economy and the government issued a number of legislations to that effect including the monetary and banking proclamation No.83/1994 and Licensing and Supervision of Banking Business No. 84/1994. These proclamations laid the legal basis for the establishment of local private banking industry in Ethiopia. Subsequently, the first private bank i.e. Awash International

Bank was established in 1994. In 1996, Licensing and Supervision of the Business of Microfinance Institution Proclamation No. 40/1996 was issued. Following the proclamations, many Micro Finance Institutions have been established. Currently, in Ethiopia, there are 19 banks (three of them are state owned), 17 insurance companies and 35 microfinance institutions.

Access to finance in Ethiopia is at low level. As stated by Global Findex database 2014, nationally, 14% of the adult population has access to formal saving and credit products. However, in rural area the rate of access to finance is 1% and there is no financial institution that offers Islamic finance for substantial number of the Muslim population who need sharia compliant finance (Bayrne and Anderson, 2015). Because of the low level of access to finance in Ethiopia and the unavailability of full-fledged interest free finance, Muslims are the double victim of financial exclusion.

Even though the cause of financial exclusion is different from country to country, lack of finance, farness of financial institution, lack of trust in financial institution and religious reasons are the most common hindering factors in accessing financial services (Demirgüç-Kunt et al., 2015). Religious factor is one of the common reasons for financial exclusion of Muslims across the world (Ben, Barajas & Massara, 2015; World Bank, 2014). In terms of population, the numbers of Ethiopian Muslims are more than the population of many Muslim countries such as Malaysia and Saudi Arabia, which are bolstering in Islamic finance industry. However, there is no full-fledge interest free finance in Ethiopia.

Ethiopian Muslims were requesting the government for the opening of Islamic finance for many years. Taking the long request in to account, the National Bank of Ethiopia (NBE) issued a Proclamation No: 592/2008 that allows interest free finance in 2008. Article 22, Sub-article 2 of the proclamation states that “The National Bank may issue directive to regulate banking businesses related to non-interest-bearing deposit mobilization and fund utilization.”

Following this directive, the first interest free bank in the history of the country had been on establishment selling shares in the name of Zamzam Bank. But the NBE issued a new directive No. SSB/51/2011 that limits interest free banking only to the possibility of opening interest free windows by conventional banks that led to the termination of the Zamzam Project. Currently, there are 8 conventional banks that are offering interest free services through window system.

The provision of interest free services by conventional banks created suspicion among Muslims who do not believe that the service is compliant with sharia principles. For Muslims who need full-fledge interest free finance, accessing interest free services from conventional banks is difficult to accept as a sharia compliant finance (Kerima, 2016). In fact, the NBE acknowledges that the service given to the Muslim is insignificant. In this regard, the vice Governor of NBE said the following in a speech he delivered during the international Islamic Banking Summit Africa in Djibouti:

> The government wants to industrialize its economy but this requires sustaining investment rates of almost 40 percent of GDP over the next five years. This can only be achieved if the financial sector, particularly the banking industry, can play significant role in mobilizing desperately needed savings from domestic sources. Islamic finance could help in this endeavor, so the central bank is conducting a study to determine the demand for sharia compliant financial products in a country where around a third of the population of 100 million is Muslim. The study would help determine what proportions of Muslims are excluded from the financial sector. If this is identified to be a barrier, a specific and enabling regulatory framework will be developed so as no one is excluded from obtaining financial services because of religious reasons. Sharia compliant financing facilities that these banks provided to their customers are even very much *insignificant* (Reuters, Nov 4, 2016).

We can understand from the above statement that NBE confirms the role of Islamic finance to enhance economic development and the current interest free services offered by conventional banks are very much trivial. In this regard, the arguments are: Ethiopian Muslims are excluded from the conventional financial services of the country due to religious reason; the newly introduced interest free banking services by the conventional banks did not meet its objective as Ethiopian Muslims prefer full-fledge Sharia compliant financial services and products. So, the main aim of this paper is to examine the abovementioned arguments based on empirical research.

### 1.2 Statement of the Problem

Islam is a comprehensive religion concerned with all aspect of human life. When we come to financial transaction, Islam prohibited dealing with *Riba* (interest), *Gharar* (uncertainty), *Maisir* and *Qimar* (Game of chance) (Ayub, 2007). According to Quranic teaching, trade is permissible and interest is prohibited (Quran: Al-baqarah: 275). However, interest is the backbone of conventional financial system (Meera, 2002). For Muslims working with conventional banking is against the Sharia principle. This results in exclusion of the Muslim population from the financial system (Sain, Rahman & Khanam, 2016).

Financial inclusion is one of the main objectives of the developing countries (Mohieldin et al., 2011). The Ethiopian government is also working to maximize financial inclusion by expanding conventional banks and micro finances (Zwedu, 2014). Contrary to this move, the NBE denied permission for the establishment of full-fledged Islamic finance. Instead, the NBE permitted interest free banking window by directive number SSB/51/2011. This means only conventional bank can provide interest free banking service. *Sheria* compliant products and services offered to customers by conventional banks are, however very insignificant (Reuters Africa, 2016). Due to the unavailability of sharia compliant financial services and products, Muslims are considered voluntary non-users of the conventional financial products and services (Thukumar and Devamohan, 2008). In 2007, insisting on the importance of opening interest free finance in Ethiopia, the Muslim Diaspora requested Meles Zenawi, the former prime minister of Ethiopia, though their request was unanswered (Feyissa, 2014).

The need for interest free finance among Ethiopian Muslims together with the lack of interest by the government to permit a full-fledged interest free banking indicate there is a gap in the financial inclusion policy in Ethiopia. This leads Ethiopian Muslims to be economically disadvantaged, marginalized and bystander in huge investments of the country.

In international level, there are a lot of studies on the topic financial exclusion. However, only few scholars such as Warsame (2009) and Mohieldin, et al (2011) conducted researches on the topic of the role of Islamic finance in tackling financial exclusion. In the case of Ethiopia where there are more than 34 million Muslims, there is no research on religious driven financial exclusion and the role of Islamic finance in tackling of it to the knowledge of researcher.

This study, therefore, endeavors to fill the gap by investigating the extent of religious driven financial exclusion and the role of Islamic finance in tackling financial exclusion in Ethiopia.

### 1.3 Significance of the Study

Through presenting scientific analysis which shows the extent of financial exclusion of Ethiopian Muslims due to the absence of alternative financial system, this paper will help policy makers to develop demand driven policy which insure financial inclusion of Muslims. Furthermore, this paper will be also used as a springboard for further research in the area. Due to the absence of adequate research in this topic in Ethiopia, the contribution of this paper for the body of literature will be also invaluable.

### 1.4 Research Questions

This study strives to answer the following main research questions:

1. What is the extent and nature of religious driven financial exclusion of Muslims in Ethiopian?
2. How is the access of Ethiopian Muslims toward the existing interest free banking services are being offerd by Conventional banks?
3. Can the introduction of full-fledged Islamic finance in Ethiopia reduce the level of financial exclusion of Ethiopian Muslims?

### 1.5 Objective of the Study

This study tries to accomplish the following main objectives:

- To assess the nature and extent of financial exclusion of Muslims in Ethiopia
- To assess the level of Ethiopian Muslims participation in the existing interest free window system
- To find out the the attitueds of Ethiopian Muslims towards full-fledged Islamic finance in Ethiopia and its role in enhancing the level of financial access to Ethiopian Muslims.

## 1.6 Motivation

Although Islamic finance is expanding in different part of the world, even in countries where the Muslim population is small like UK, Australia, Kenya which are using Islamic finance and Islamic fund to include their Muslim citizens in the financial system, Ethiopia, with more than 34 million Muslims, has not yet allowed the establishment of full-fledged interest free finance except interest free window services exclusively offered by conventional banks.

Considering this fact, Thukumar and Devamohan (2008) notes:

> The National Bank of Ethiopia should study the experiences of other non-Muslim countries which have Islamic banks, for instance Britain, United States, etc. It is observed that there are 1.8 Million Muslims in England, and there were Islamic funds and Islamic financial institutions. Ethiopia has definitely more than 10 times higher than England's Muslim population. So, it is justified that Ethiopian Muslims should have an Islamic Bank (P. NA).

It is this reality and tangible gap which motivate the researcher to carry out this scientific study, i.e. to know the extent of religious driven financial exclusion and to assess the role of Islamic finance in tackling of financial exclusion.

## 1.7 Organization of the Paper

This paper is classified into six parts. Introduction, research background, statement of the problem, significance, research questions, objectives, motivation and organization of the study are covered in the first part. The second part dedicated to theoretical perspectives and literature reviews about financial exclusion and Islamic finance. Research design and methodology, sampling technique, data collection instruments, method of data analysis are presented in part three. In the fourth part, findings and analysis of this study are presented. The fifth part of the study presents the discussion of findings based on literatures. Finally, the last part deals about the conclusion and recommendations of the study.

# 2 LITERATURE REVIEW

## 2.1 Introduction

This chapter dedicated to review different literatures on the area of financial exclusion and Islamic/interest free/ *sharia* compliant finance. In the first part of this chapter, definition of financial exclusion, basic financial services, causes of financial exclusion, consequences of financial exclusion, measures to tackling financial exclusion and financial exclusion in Africa in general and in Ethiopia in particular are covered. In the second part of this Chapter, the position of finance in Islam, historical development of Islamic finance, products and services of interest free bank, Islamic insurance/*takaful* and Islamic microfinance, Islamic finance in Ethiopia and the role of Islamic finance in tackling of financial exclusion are reviewed.

## 2.2 Financial Exclusion

There is an increase in assessing, apprehending, and confronting financial exclusion around the globe. The concept of Financial Exclusion has been gaining attention in developed countries from 1990s (Warsame, 2009). Different scholars define financial exclusion based on different contexts. Anderloni et al. (2008) defines financial exclusion depending on difficulties to access finance. "Financial exclusion refers to a process whereby people encounter difficulties accessing and/or using financial products and services in the mainstream market that are appropriate to their needs and enable them to lead a normal social life in the society in which they belong" (p.9). In addition to this, Leyshon and Thrift, (1995) also defined financial exclusion as a process of excluding poor's and disadvantage groups because of fearing risks. Further, Link (2004) stated that, financial exclusion is the absence of access to financial products and services by single person or societies due to their geographical location. According to Connolly et al., (2011) "Financial exclusion exists where individuals lack access to appropriate and affordable financial services and products – the key services and products are a transaction account, general insurance and a moderate amount of credit" (p.6). In general, Kempson, et al. (2000) identified different dimensions of financial exclusion. These dimensions are summarized in the table below.

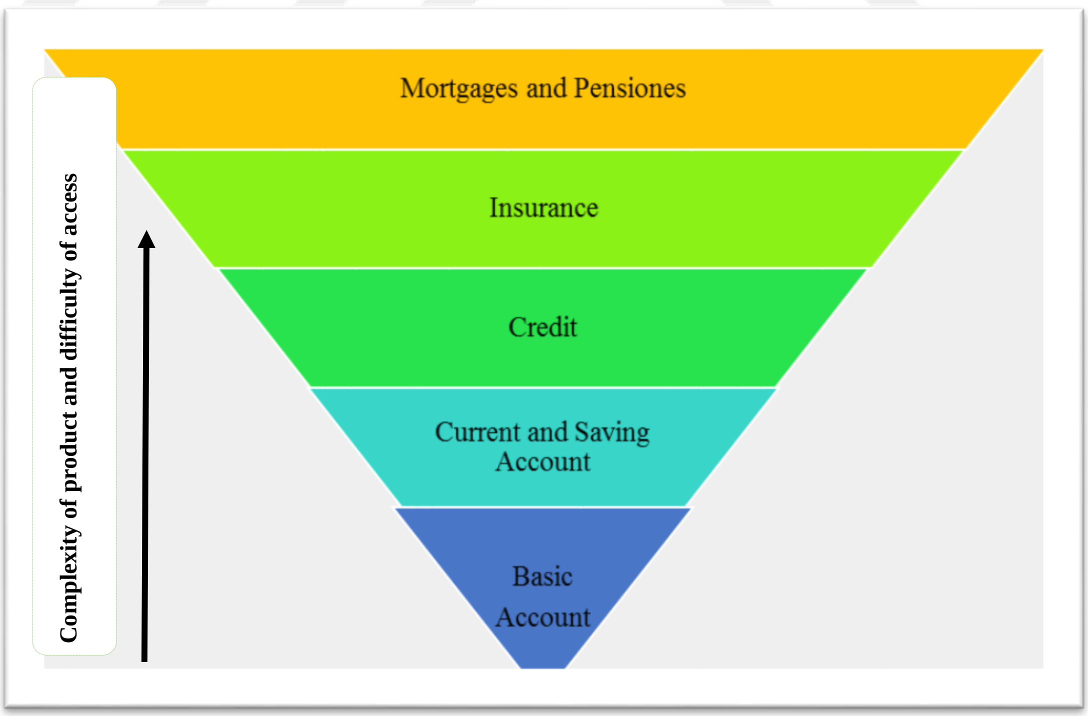
Table 2.1 Dimensions of Financial Exclusion

| Dimensions | Definition |
|---|---|
| Access exclusion | The process of risk assessment may exclude some people. |
| Condition exclusion | The exclusion resulted from conditions put by financial institutions. |
| Price exclusion | The cost of financial services may be affect some people. |
| Marketing excludes | Exclusion resulted from the marketing strategy of financial institutions. |
| Self-exclusion | People not used conventional banks because of religious reason. |

### 2.2.1 Basic Financial Services

According to World Bank (as cited in Anderloni et al. (2008) and Blake and Jong (2008), the basic financial products and services considered to be essential for all societies are transaction banking (Basic accounts), saving, credit and insurance.

Figure 2.1 A pyramid of Basic Financial Products




Source: Adapted from Blake and Jong (2008)

**Transaction Banking**: The access of basic transaction banking services is essential need in the universal level. There are several types of services linked to transaction banking, such as receiving electronic payment like wages and pensions, converting cheque, storing money, paying for goods and services without cash, paying bill electronically and making remittances. Not having access or use of these services had an impact on social inclusion, difficult, expensive only using cash and increase the chance of risk (Anderloni et al, 2008).

As reported by Demirgüç-Kunt et al. (2015), worldwide 62% of adults have account. In high income Organization for Economic Co-operation and Development (OECD) economics 94%, in developing countries 54% of adults own account. In developing economies, the range of reported as having account is from 14% in Middle East to 69% in East Asia and Pacific. This shows that, 6% adults in high income economies, 31% adults in Middle East and 86% adults in East Asia and Pacific are reported as not having account.

**Saving**: Saving accounts are important to smooth consumption when earning or expenses varies over time. The problems of excluding from accessing saving in financial institutions are exposed to loan sharks in times of emergency and to smooth expenditures and difficult to acquire assets or investments or to become a home owner (Blake and Jong, 2008). In International level, 44% of adults are had not save in 2014. In East Asia and Pacific, Europe and Central Asia, High-income OECD Economies, Latin America and Caribbean, Middle East, South Asia and Sub-Saharan Africa, 29%, 62%, 29%, 59%, 70%, 64% and 40% adults respectively are reported that they had not save (Demirgüç-Kunt et al.,2015).

**Credit**: Credit is the main financial product that enables to access goods or expenditures that are the key parts of monthly budgets. It also plays a significant role to smooth consumption and unexpected financial needs (Anderloni et al, 2008). The Global Findex database 2014 reported that the percentage of adults borrowing from formal and informal financial sources. Worldwide, 42 % of adults reported they had borrowed money. In regional level, 41% in East Asia and Pacific, 40% in Europe and Central Asia and High-income OECD Economies,33% in Latin American and Caribbean, 46% in Middle East, 47% in South Asia and 54% in Sub-Saharan Africa adults borrowed from any sources of finance (Demirgüç-Kunt et al.,2015).

**Insurance**: Insurance is one of the essential financial products to restore the lost assets in the events of crisis of natural catastrophe and human made risks (Blake and Jong, 2008).

### 2.2.2 Who are Financially Excluded

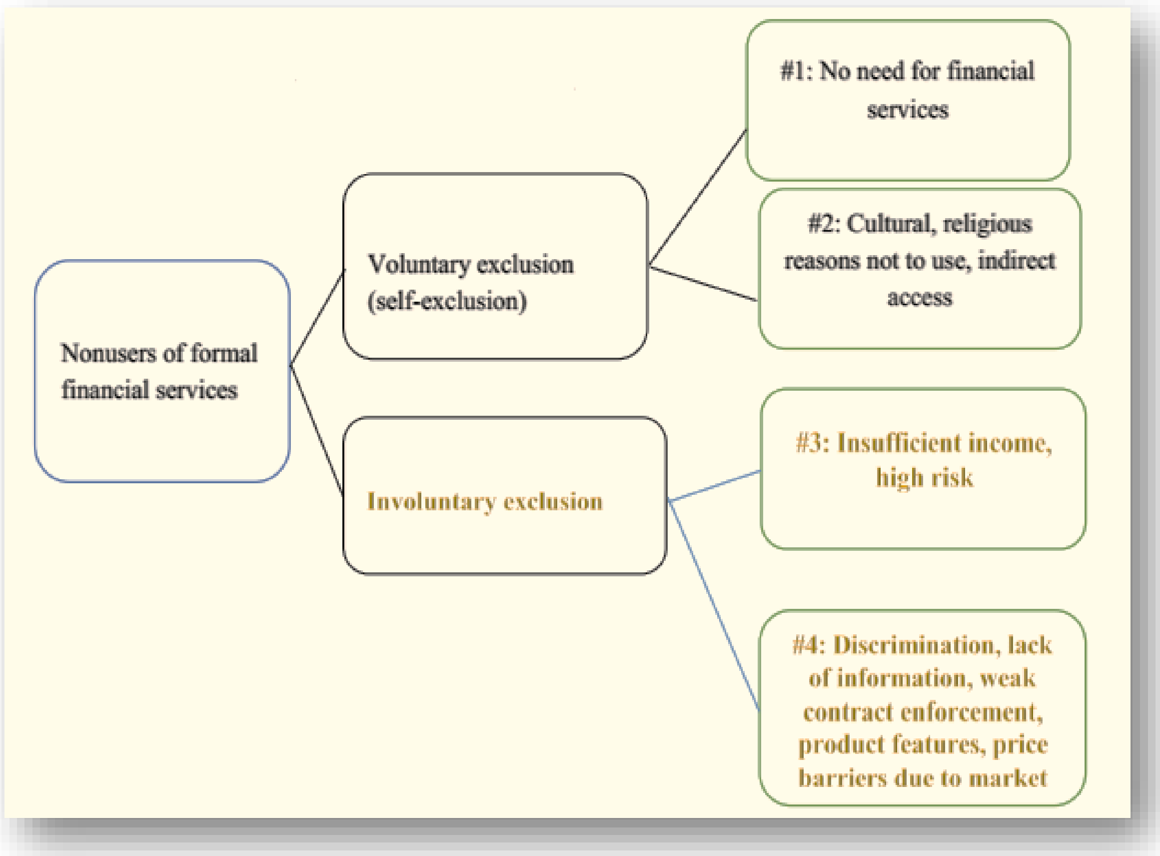
Financial exclusion influences 2 billion people in the world and 350 million people in sub-Sharan African countries (Demirgüç-Kunt et al.,2015). The number and case of financially excluded people are different from continent to continent and country to country. As stated by Demirgüç-Kunt et al. (2015), in 2014, the number of unbanked by region is as follows. High-income OECD countries 3%, Middle East countries 4%, Europe and Central Asia 4%, Lain America and Caribbean 10%, Sub-Sharan Africa 17%, East Asia and Pacific 24%, and South Asia 31% of their population are unbanked. In regional classification, South Asia, East Asia and Pacific, and Sub-Saharan countries are the home of financially excluded inhabitants.

In case of individual level, constantly the same groups of people are excluded from finance. People with unstable income source, unemployed or who do not have permanent work, low asset owners, migrants, people who have a history of unpaid debt, and religious people are the most common financially excluded people (Warsame, 2009). In Africa, the people who live in rural areas are more affected by financial exclusion than the people who live in urban area (Triki and Faye, 2013). Kempson and whyley (1999) find out that, households that have never used financial products and services for a lengthy period includes elderly people with low income, young households, single mothers, marginalized workers and ethnic minorities. Contemporary researches are demonstrating Muslims are financially excluded in countries in which only conventional financial system is applied. According to Demirgüç-Kunt et al. (2015), in Muslim dominated countries like Niger, Turkey, Turkmenistan, and Uzbekistan 25% of adults are excluded from the financial service because of religious reason.

### 2.2.3 Causes of Financial Exclusion

The causes of financial exclusion are different from country to country and from people to people. Based on the global findex survey questionnaire gives 150,000 respondents in 148 countries who have not account in financial institution, lack of sufficient money to open account (30%), having account too expensive (25%), one among the family members already have an account (23%), the financial institutions are very remote (20%), unavailability of required documentation (18%), lack of confidence on the financial institutions (13%), and religious reason (5%) are the most common causes to be unbanked (Demirgüç-Kunt et al.,2015). The global financial development report 2014 also classifies the cause of financial exclusion in four categories and these four categories have two forms, voluntary exclusion (self-exclusion) and involuntary exclusion (World bank, 2014).

Figure 2.2 Causes of Financial Exclusion




Source: Adapted from World Bank (2014)

The causes of financial exclusions are divided in to three main categories, viz. societal, supply and demand factors (Anderloni et al, 2008).

**Societal factors of financial exclusion**: The societal factors of financial exclusion address by different authors. Anderloni et al (2008) identified the following as the main societal factors affecting the access and use of finance. These factors include liberalization of financial services, labor market changes, and money laundering rules, fiscal policy, social assistance, demographic changes and income inequalities. As stated by Mitton, 2008; Kempson et al, 2000; Collard et al, 2001 (cited in Sain, Rahman, & Khanam, 2016), self-exclusion is one of the main societal factors which are hindering financial inclusion. This implies psychological and cultural hindrances in expansion of financial services and products when the less wealthy society thinks that financial services are "not for people like us". Sain, Rahman, & Khanam (2016) argued that, religious and cultural reasons are the key factors of self-exclusion from accessing finance. These reasons are recognized as the most hard and predominant barriers that keep away unbanked societies from finance.

**Supply factor of financial exclusion:** Supply factors of financial exclusion are resulted from unavailability of financial institutions in remote areas, conditions attached to financial products and expensiveness of financial products (Kempson and Whyley, 1999). Refusals of individuals by financial institutions from accessing finance is a very common supply factors because of unavailability of good credit history, lack of stable employment patterns, low income and lack of identity cards is a very common supply factor (Anderloni et al., 2008).

**Demand factors of financial exclusion**: The exclusion of some people from accessing finance because of cultural and psychological factors is known as demand factors of financial exclusion. For example, illiterates, elderly people (cash generations). Migrants and people with low incomes are think that banks are not for them and fear losing control of their money and therefore they distrust them and they seek other ways to carry out their finances (Anderloni et al, 2008). In addition to elderly people, young people are also worrying in using modern technologies to manage their financial transactions like internet banking, because of online fraud (internet hackers). This is reasonable for a certain people for not accessing of some financial services and products (Mitton, 2008).

### 2.2.4 Consequences of Financial Exclusion

The consequences of financial exclusion are affecting people's ways of consumption, ways of engagements in the economy, means of accessing social welfare, distribution of income and wealth and in general it affects the overall quality of life (Anderloni et al, 2008). Furthermore, Blake and Jong, (2008) stated that, financial exclusion affect individuals, interrupts families and encumbers society in general. It makes living on low income too difficult, unbalanced and worrying than it otherwise would be, and acts as a hindrance to personal development and economic growth.

As stated by Mitton (2008), some effects of financial exclusion are:

- ❖ Expose people to high-interest credits: This indirectly effects on a person`s mental health, because of the debt problems can cause stress, depression and feel sense of insecurity. It may also make difficult to go to work, as people on means-tested benefits who have high amount of debt can face the expectation that their income will be taken to their creditors.
- ❖ Expose peoples to monetary crisis: This result unpredicted event like burglary or flooding.
- ❖ Excludes people from bill paying facilities: individuals, who have not bank accounts pay more charges for most of utility suppliers by using other methods of payments like pre-payment, pay out card and postal orders or cash. "The poor pay more" in this increasingly cashless economy.
- ❖ Expand social exclusion: It is not an individual problem, instead; the whole community can suffer from under investment in financial services.

### 2.2.5 Measures to Tackling Financial Exclusion

The lives of billions of people have been affected due to financial exclusion in worldwide. The developed world countries are partially filling the gap by new innovations and technology advancement. In the developing world, the unavailability of adequate and suitable financial institutions and financial sources are the factors behind the expansion of financial exclusion (Warsame, 2009). According to Anderloni et al (2008), the market policy approach to tackle financial exclusion, profit oriented and non-profitable financial institutions should:

- ✓ Develop new products and services,
- ✓ Work in partnership to widen access and reduce costs, and

- ✓ Participate in financial education and advice.

Anderloni et al (2008) suggests that to overcome financial exclusion, regulators ought to develop a system that create a room to provide incentives when peoples exposed to difficulties by using and accessing finance from sub-prime markets; and illegal lending such as loan sharks should be controlled and stooped. In addition to this Blake and Jong (2008) recommended the following solutions to tackle financial exclusion.

- Improving the financial capability of peoples: This includes educating of peoples regarding to some financial knowledge and skills, such as planning, budgeting and giving practical support to access financial products and services.
- Tackling poverty: there is a cause and effect relationship between poverty and financial exclusion. Lobbying government and campaigning to income maximization and poverty reduction are their own effect in talking of financial exclusion.

Furthermore, provision of easily accessible banking service, increasing affordable credit services, and providing of social funding by state are important to overcoming demand side credit exclusion (Anderloni et al, 2008).

### 2.2.6 Financial Exclusion in Africa

Developing regions are home for the majority financially excluded peoples. In developing region 46% and 60% of youths do not have account and not save respectively (Demirgüç-Kunt et al., 2015). Financial systems in Africa are underdeveloped and their accessibility is very limited. Low and unstable income level, inflationary environments, high illiteracy rates, insufficient infrastructure, government challenges and the limited competition in the banking industry as well as excessive cost of banking are some factors used as the cause of underdeveloped financial systems and its limited accessibility (Demirgüç-Kunt and Klapper, 2013). In Africa, people living in rural area, poor, women, less educated adults, young and older adults are the most financially excluded groups.

According to the global findex database, that covers 42 African countries available in 2012, 77% of adults in Africa have not account in formal financial institution. There is a large variation of unbanked in Africa, from 68% in Southern Africa to 95% in Democratic Republic of Congo and Central Africa Republic. The most frequently cited barriers (80%) to having formal account in Africa is lack of enough revenues. In addition to this cost, distance, insufficient documentation, poor infrastructure and telecommunication, heavy branch regulations and strict geographical expansion of banks are the main barriers to having formal account in Africa (Demirgüç-kunt and Klapper, 2013).

The current growth of mobile money, it is known as Branchless Banking has offer for millions of excluded people from formal financial system the chance to access financial services relatively cheap, securely, and reliably. Overall in Africa, 14% of adults were using mobile money in 2012. In Africa 36% of adults cite as having saved or set aside money. In case of borrowing, 44% of adults reported as having borrowed money from formal and informal financial institutions. This is more than the worldwide rate of 34%. The use of insurance product remains limited in Africa. Only 3% are reported having health insurance and only 6% of those who work in farming, forestry or fishing industries report having purchased crop, rainfall of livestock insurance (Demirgüç-kunt and Klapper, 2013).

Concerned various stakeholders with combating financial exclusions proposed some solutions to overcome financial exclusion in developing world. Among the proposed solutions:

1. Establishing Appropriate financial infrastructure: Government should examine optional systems of documenting individuals` credit history, promote advanced means through which people can get credits, encourage regional financial integration between countries within common geographical areas (Oji, 2015).
2. Enhancing informal financial systems and Micro-financing: In Africa, many people use informal financial systems such as Rotating Saving and Credit Associations (ROSCAs), tontines, chit funds and burial societies (Demirgüç-kunt and Klapper, 2013). These informal financial institutions are important to overcoming the problems faced by formal financial institutions including asymmetries of information and collateral. The promotion informal financial institutions by adding some features is very important to enhancing financial exclusion in developing countries when formal financial institutions failed. (Warsame, 2009).

3. Diversify product offering: Government in developing countries should encourage competition between financial institutions with the innovation of financial products and services that can address the needs of financially excluded societies. For instance, the expansion of Sharia compliant financial services is the only way to include Muslims who are not accessing conventional financial services because of religious reason (Oji, 2015).
4. Promote financial literacy: Understanding financial products and services are one of the motivator that enables people to manage their money and access financial services. As stated by Oji (2015), many rural peoples of Africa are not having basic knowledge regarding to finance. Promotion of financial literacy is important for financial inclusion.

### 2.2.7 Financial Exclusion in Ethiopia

Global financial inclusion (Global findex) database drawn a survey from 150.000 people around the world in 140 countries. Ethiopia is one of the countries included in this survey. The survey was used 1004 Ethiopians as a sample size. In the report, 78% of adults had no account in formal financial institutions, 86% of adults were not having formal saving, and 93% of adults had not taken formal borrowing. This shows that majority Ethiopian people are excluded from formal financial institutions. In addition, the performance of financial inclusion is lower than Sub-Sharan countries average (Demirgüç-Kunt et al., 2015).

The 2016 Brookings Financial and Digital Inclusion Project report (FDIP) done by Center for Technology Innovation (CTI) at brooking measured 26 countries financial performance by four dimensions, such as country commitment, regulatory environment, mobile capacity and the adoption of traditional and digital financial services. According to this report, Ethiopia is ranked 25$^{th}$ from 26 countries and get 53% overall score. Mobile banking is one of the driving forces of financial inclusion in sub-Sharan countries. However, Ethiopia has the lowest level mobile capacity and adoption (Villasenor, West and Lewis. 2016).

Formal financial institutions in Ethiopia which are providing service for people are commercial banks, MFIs and insurance companies. There are 18 commercial banks and one state owned development bank in Ethiopia. The total numbers of branch of all commercial banks are 2,972. This mean, in Ethiopian one commercial bank branch is serving 31,024 people on average. In addition to this 35.4% from the total branches are found in urban area (Villasenor, West and Lewis. 2016). However, 80% of Ethiopian population inhabited in rural area. This means rural populations are highly excluded from accessing commercial banks services. As stated by Zewdu (2014), in 2014, there were only 31 MFIs with 1385 branches and sub branches providing financial services in Ethiopia. The ratio between one MFIs branch and numbers of population is one branch to 61,228 people. 14 (45%) of them provide service in Addis Ababa. In 2011, all MFIs provided credit for only 2,470,641 clients. This numbers are insignificant comparing to the number of Ethiopian people (Deribie, Nigussie and Mitiku, 2013).

There are 17 insurance companies in Ethiopia. One state owned and 16 privete share companies in 2014. They have 332 branches in Addis Ababa and regional cities. 55% insurance companies' branches are providing serves in Addis Ababa. The rest 45 % of branches are operating in different regional cites. In the country level, there is only one insurance branches within the area of $1000KM^2$. (Jarso, Rao and Ravi, 2015). Most Ethiopian peoples are not accessing insurance services especially in the rural area.

#### 2.2.7.1 Causes of Financial Exclusion in Ethiopia

The followings are identified by different scholars as a cause of financial exclusion in Ethiopia.

1. Lack of Information technology infrastructure and innovation: Even though the NBE issued different directions to enhancing banks to use different modern technologies, the problem is not solved. For instance, mobile banking is one of the driving force to financial inclusion in Africa. However, Ethiopia is still at lower level comparing to other African countries. The main hindrance for the expansion of technology based financial services is critical and continuous frequent breakdown in internet services and energy. These two sectors are controlled by the government. This creates the absence of competition to solve the problems. As stated by Worku, Tilahun and Tafa (2016); Hussen, (2015) and Worku (2010), low level of internet access, relatively

excessive cost of internet and continuous power interruption of power are the main challenges in the expansion of mobile and internet banking in Ethiopia. Lack of innovation of new products and services are also one of the main problems in Ethiopia (Zegeye, 2014).

2. Lack of physical access: The numbers of population and financial service providers are not balanced. The outreach ratio of one bank, insurance and MIFIS are 31,024, 61,288 and 277,720 people respectively. In addition to this, most financial service providers are concentrated in cites while, 80% of the populations are in the rural area (Deribie, Nigussie and Mitiku, 2013).

3. Financial regulation: The financial regulation of Ethiopia also affects the establishments of new financial institutions. For instance, NBE issue a new directive, known as "Minimum Capital Requirement for Bank No.SBB/50/2011". In this directive, the minimum paid up capital to get a banking license raised from 75 million Ethiopia birr to 500 million Ethiopian birr. For MFIs, the minim paid up capital in 1996 was 200,000 Birr (Directive No. MIF/01/96). This amount rose to 2 million Birr in 2013 (Directive No. MIF/25/13). Finally, the minimum paid up capital raised to 10 million Birr by Directive No. MIF/27/2015. This means the minimum paid up capitals of banks and MFIs are increased by 666% and 5000% respectively. Strong paid up capital is important for financial institutions to absorb losses and to protect depositors from unforeseen risks. However, it is difficult the establishments of new banks and MFIS providing this paid-up capital and even some under foundations are closed because of high startup capital (Zewdu, 2014). In addition to this in Ethiopia the establishments of full fledge interest free banking is prohibited by SBB/ 51/2011. Interest free finance have a significant role to enhance financial inclusion by providing financial services for those who are excluded from accessing conventional financial services because of religious reason. Another problem regarding to financial regulation is commercial banks conservative lending policy. To access finance from commercial banks every customer should pass by the process of "know your customers" (Zewdu, 2014). Majority of people do not pass this process and are rejected by banks. Foreign financial institutions are also not permitted to participate in financial sector in Ethiopia

(Hussein, 2015). This is one of the causes to low competition and innovation between local financial institutions.

4. Shortage of loanable fund: The shortage of credit products and prohibition of credit for smoothing consumption, income and investment is among the challenges of accessing credit in Ethiopia (Radzewicz-Bak et al., 2015). Ethiopian Public Private Consultative Forum (EPPCF) in 2014 puts access to finance is one of the top challenges of business environment and from 1000 credit applications only 2 were acceptable in Ethiopia (Zegeye, 2014).
5. Lack of financial literacy: One of the demand side causes of financial exclusion in Ethiopia is low level of financial literacy in the rural area (Zegeye, 2014).
6. Collateral requirement: Commercial banks are asking collateral that the value of which more than the credit amount asked and, they prefer to provide credit for large volume borrowers to easily control (World Bank, 2009 cited in Zewdu, 2014). As stated by Zegeye (2014), Banks in Ethiopia are asking collateral 2.4 times of the loan value.
7. Religious Reason: Ethiopian Muslims are not using the conventional financial products and services because of the inaccessibility of sharia compliant financial services and products (Thukumar and Devamohan, 2008).
8. Poverty, low income: according to the survey done by Rao and Baza (2017), lack of money is one of the main causes to financial exclusion in Ethiopia.

#### 2.2.7.2 Financial Inclusion Initiatives in Ethiopia

Financial inclusion is one of the weapons of promoting economic development and tackling poverty (Radzewicz-Bak et al., 2015). To enhancing financial inclusion, the government of Ethiopia has been doing several attempts. Among them:

1. National Bank of Ethiopia adopts Maya Declaration: Maya declaration is a declaration made by of network of central banks, supervisory and other financial regulatory bodies who met in Riviera, Maya, Mexico between 28-30 September 2011. The conference was in organized by Alliance for Financial Inclusion (AFI). In this declaration, the members of AFI recognize the significance of financial inclusion to empowering and

transforming the lives of peoples, in improving monetary crisis and the contribution inclusive it has growth in developing and emerging market countries. Members are agreed to set financial inclusion policy that makes full use of suitable innovative technology at low cost, execute a sound regulatory frame work that can achieve the goals of financial inclusion, stability and integrity, recognize consumer protection and empowerment and making evidence based financial inclusion policy by collecting and analyzing inclusive data, track the profile of changing of financial inclusion and producing indicators (Maya Declaration, 2011). In this regard, NBE reports some policy area of commitment in 2015. Financial literacy and credit information system are reported as completed and national payment system, housing finance, national financial inclusion strategy; digital financial services are reported as they are in progress (AFI, 2015).

2. Regulation of Mobile and Agent Banking Services: mobile banking is play a significant role in enhancing financial inclusion in Africa. Even though there is a limited internet and power interunion barriers in Ethiopian, NBE issued directives No. FIS/01/12 for financial institutions to conduct mobile and agent baking service.
3. Financial Inclusion Council (FIC): NBE established Financial Inclusion Council (FIC) to enhancing financial inclusion in the country. The main aim of establishing FIC is to unify financial inclusive services offering by different bodies (Tadesse, 2014).

### 2.2.8 Religious-Driven Financial Exclusion

This paper is concerned only on specific aspect of financial exclusion; religious-driven financial exclusion. The researcher has not found any specific definition of religious driven financial exclusion. But, it may be defined as a type of financial exclusion resulted from the absence or lack of financial products and services which are compliant with religious principles. Recently, all countries around the world adopted conventional financial system. Some features of this financial system are not acceptable by a certain group societies. For instance, interest is strictly prohibited by the three Abrahamic beliefs, i.e. Judaism, Christianity and Islam (Meera, 2004). However, only Muslims are traying to observe their religious principle regarding to the prohibition of interest. According to the study done by Demirgüç-kunt, Klapper and Randall (2014), with a sample of over 65,000 adults from 64 economies, representing 75 percent of the world's adult Muslim population, the result shows that Muslims are more likely than non-Muslims to report religion as a barrier to account ownership. Furthermore, different studies such as Sain, Rahman, & Khanam (2016); Zulkhibri, (2016); Gaisbauer, Schweiger, & Sedmak, (2016); Redin, (2015); Tomalin, (2015); World Bank (2014) and Adewale, (2014) identified religious reason as a cause of financial exclusion of Muslims. This is because of the fact that conventional financial services are against sharia principle.

### 2.2.9 Religious-Driven Financial Exclusion in Ethiopia

The researcher could not find any research conducted on the topic of religious driven financial exclusion in Ethiopia except the speech of vice governor of NBE, Getahun Nana. He said that the NBE is conducting a study on the demand of sharia compliant financial services and this is important to know the extent of Muslims excluded from the financial sector (Reuters Africa, 2016). Even though, there are several indicators in the existence of religious driven financial exclusion. For instance, the main reason to issued SSB/51/2011 directive by NBE was the strong public demand for interest free finance products in Ethiopia.

## 2.3 Islamic Finance

The term *Islam* is an Arabic word which denotes peace, surrender and obedience. The religion of Islam is antique as humankind itself. It is the religion of all prophets from Adam to Jesus and the last prophet Mohammed peace be up on them all. Anyone who accept Islam means he surrender himself to Allah. The followers of Islam are known as Muslims. Allah created all things within this word and regulate how humankinds deal with him and with other creations. He teaches humankind by sending messengers and by revealing holly books. The final messenger is prophet Muhammed (PBUH) and the last holly book is *Quran*. The teaching of Islam is not limited by only well-known worshiping activates such as prayer (*Salat*), fasting (*Sawm*), pilgrimage (*Hajj*) and almsgiving (*Zakat*). Instead, it encompasses all aspects of human life. If a Muslim does his day-to-day activities based on Sharia principles, with good intention and for the sake of Allah, he will perform worshiping.

The primary sources of Islamic jurisprudences are Quran and the sayings and the actions done and /or approved by holy prophet (*Sunnah*). The supplementary sources are the unanimous consensus of companions of the prophet or Muslim scholars on a point of Islamic law (*Ijma'*) and analogical deduction of Islamic law (*Qiyas*) (Philips, 2006 and Ayub, 2007).

The rulings of *Sariah* encompass every religious issue that determine the conduct of a Muslim toward himself, family, neighbors, society and the Muslim community as well as the environment in general. The purpose of *Sariah* is to help humankinds be successful and promote happiness in this world and the hereafter by performing good things that are ordered by sharia and far from dreadful things prohibited by Sharia. By an inductive survey of *Quran* and *Sunnah*, Muslim Jurists like Abu Hamid al-Gahzali (111 CE), Imam al-Shatibi (1388 EC) and Tahir ibn Ashur (1907 CE) identified the objectives of Sharia (Auda,2008). These objectives are classified as primary and secondary objectives. As stated by Ayub (2007), the primary objectives of Islam are Preservation and protection of:

1. Religion,
2. Life,
3. Progeny- family unit
4. Property,
5. Intellect and
6. Honor (P.23)

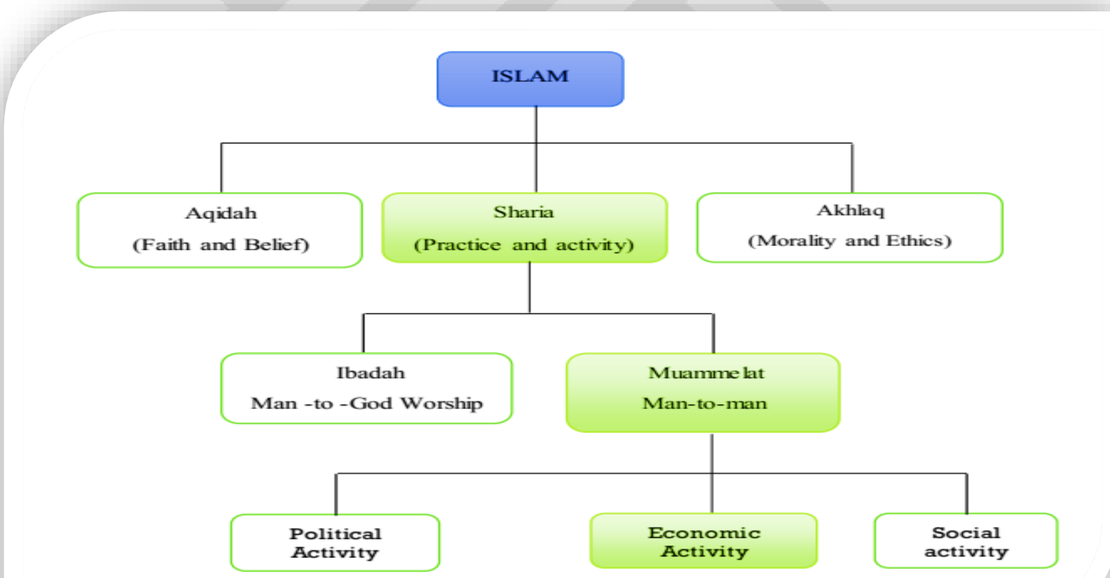
Further, Ayub (2007) stated the following secondary objectives of *Sharia:*

1. Establishment of justice and equity in society,
2. Promotion of social security, mutual help and solidarity,
3. Maintenance of peace and security,
4. Promotion of cooperation in good matters and prohibition of evil deeds and actions,
5. Promotion of supreme universal moral values and all actions necessary for the preservation and authority of nature (P.24).

Muslim scholars and Islamic institutions describe the position of economics and financial issues in Islam. Bank Islam Malaysia (2011), Rosly (2005) and Anas, Dahan and Yaacob (2016) describe that Islamic law (*Sariah*) consists three basic categories viz. *Aqidah (*faith, belief*), Sharia* and *Akhlaq (*ethics, morality*). Sharia* is an Arabic word, which refers to a straight path. Technically Sharia defined by Philips (2006) as "the sum total of Islamic laws which were revealed to the Prophet Muhammad, and which are recorded in the Quran as well as deducible from the Prophet's divinely-guided lifestyle called the *Sunnah*" (p.16).

As described in figure 2.3, Shariah consist of two basic elements such as *Ibadah* (the relationship between creator and human) and *Muamalat* (the relationship among human and human). The rulings regarding to *Aqidah, Akhlaq* and *Ibadah* are fixed and performed in every time and places with the same standards. However, *Muamalat* required *Ijtihad* (adjudication) because scholars deduce this rules from *Quran* and *Sunnah.* The position of Islamic economics and financial issues in *Sharia* as one major category of *Muamalat* which are issues that arise between humans and human with other creatures (Shanmugan and Rina, 2009).

Figure 2.3 The Position of Finance in Islam



Adapted from Bank Islam Malaysia

Economic issues are one of the major part of *Muamalat.* Trade and transaction, selling of assets, sale of payment in advance(*Salam*), loans, mortgage, guarantee, suretyship, transfer of debts, commissioning, *mudarabah*, renting and hiring and other issues are the Economic issues of Islamic doctrine (Al-Fawzan,2005). The above mentioned Islamic Economic issues are done by either Islamic banking, Islamic Insurance or Islamic micro finance institutions.

### 2.3.1 Historical Development of Islamic Finance

The foundation of Islamic finance goes back to the era of Prophet Mohammad (PBUH) before 1438 years ago (Alharbi, 2015). As noted by Chapra and Khan (cited in Chachi, 2005), from the era of Prophet (PUBH), Muslims could establish interest free financial system for resource mobilization to funding productive activates and basic needs. The method was mainly depending on profit and loss sharing mode of financing i.e. *mudarabah* and *musharakah*. In the following table, Islamic financial instruments existed from the rise of Islam until 12th century are summarized.

Table 2.2 Islamic Financial Products Existed Since the Rise of Islam

| | |
|---|---|
| *Byta al-mal* | It is an Arabic word refers to house of money or house of wealth. Possumah and Ismail (2012), noted that "Bayt al mal performs as a treasury of Islamic state with the activates of planning and distributing of society's wealth in the socio economic and political system of within that state" (p.28). Bayt al mal, which was the central bank of Islamic states and its key role were supporting poor. Its source of income was Zakat (alms), land tax, donation and property without owners (Mohamad, Abdullah, Mohamad, and Abidin, 2013). |
| Money order | This one of the financial activity takes place in the early Islamic era. For instance, the companion of Prophet (PUBH), Ibn Abbas had once received *Warik* (a type of currency made from silver and turned in to dirham) and wrote the voucher of acceptance to Kufah (Mohamad, Abdullah, Mohamad, and Abidin,2013) |
| Bill of Exchange | The companion of Prophet (PUBH), Abdullah bin Zubayr once received money from the people of Mecca, and he wrote the confirmation receipt to be sent to his brother in Iraq, where the owner of the receipt can re-claim their money there (Mohamad, Abdullah, Mohamad, and Abidin,2013). |
| Accepting Deposit | One of the well-known companion of Prophet (PUBH), Zubair Ibnul Awam was accepting deposit from people and he was used the money for investment. When he passed away, his liability had reached 2.200.00 *dinnar* as calculated by his son Abdullah. He had many branches in different part of Islamic empire (Alharabi, 2015). |
| Using of Cheque | As noted by Hamoud (cited in Mohamad, Abdullah, Mohamad, and Abidin, 2013), Sayf al-Dawlah al-Hamdani (970 A.D) was the first person in Islamic finance history by using of cheque. |
| Bank | Bank known *Sarrafeen* and Dawawin al-jahabidah: Chachi (2005) noted that:"The historical writings of al-Qalqashandi (1913), al-Djahshiyari (1938), Pellat and Schacht (1965), al-Kubaisi (1979), al-Ali (1953.1981), al-Sa`di (1985), al-Duri (1986,1995), Fischel (1992), al-Hamdani (2000) and Chapra and Ahmed (2002) show that there were indeed banks called *sarraffeen* or s*ayarifah* or *jahabidhah* and banks called *dawawin al-jahabidhah*." (P. 10). |

Because of continuous deviation from Sharia in political scope, extravagance of the courts, lack of organization, political breakdown, the rise and developments of different antagonistic sects, wars with crusaders, Mongols and Tatars and the Turco-Persian war, the Muslim world lost its technological and economic activity. Consequently, several Islamic institutions including Islamic financial institutions were replaced by western institutions (Chachi, 2005).

In the era of Ottoman Turkish Empire (1301-1922), Islamic financial products were limited (Naveed, 2005). The well-known Economist, Siddiqi defined the Ottoman era as "*stagnation took the Muslim mind in its grip*" (Islahi, 2007). In this era, financial activities especially *sarrafs (*money changing) were done by minority non-Muslim Greeks, Armenians, Jews and Levantines (Agoston and Masters, 2008). Since the $11^{th}$ century, trade shifted from Muslims to Europeans who become traders in the Mediterranean Sea (Chachi, 2005).

Vogel and Hayes (Cited in Chaci, 2005) discussed the situation of Muslims in $19^{th}$ century like this:

> "From the middle of the $19^{th}$ century, nearly every Muslim country, under direct or indirect pressure from the newly dominant west, adopted laws and legal systems based on Western models, particularly in the civil and commercial spheres. The centuries-old practice of finance in Islamic form was largely eclipsed. Under the European influence ` most countries adopted Western inspired banking system and business models and abandoned Islamic commercial practices. With the achievement of independence` the nationalization of foreign banks and the development of national banking` the overseas colonization of the banks disappeared` but it has been replaced by a very similar `neo-colonial` banking system. It is true that by nationalizing foreign banks and by establishing new indigenous banks, the banks became national banks, looking after the national interests, but their operating system were the same as the foreign ones in that they continued to operate and deal in interest which is alien to the belief of the Muslim population" (p.15).

As stated by Nassir, cited in Alharabi (2015), When European banking system applied in all Muslim countries, Muslim society and Scholars have three different opinions. The first group suggested that, accessing conventional banking is *halal*, the second group idea is conventional banking model is *haram*, but it is important. So, this group suggests that establishing banking business based on European model is not *haram*, and the third group opinion is banking is necessary and *rib*a is *haram.* The advocator of this argument suggested that we have several types of contract in our *sharia* that can be applied in banking business without interest, so we can establish interest free banking system. Finally, in 1940s, the idea of establishing interest free banking gained momentum in theory. This is the starting point to modern Islamic finance.

### 2.3.2 The Emergence of Modern Islamic Finance

Islamic finance has developed in recent times to create a connection between the activity of financial institutions and Sharia principles which provide alternative sharia compliant financial services (Tiby and Grais, 2015).

Alharabi (2015), classified the development of modern Islamic finance in to three phases. These three phases are summarized in the following table.

Table 2.3 Phases of the Development of Modern Islamic Finance

| Phases | Explanation |
|---|---|
| The first phase: Islamic finance under theoretical work (1930-1963) | In this phase, different scholars write on the topic of interest free finance. Among these writers, Alharabi (2015) states the following writers: "Abul Ala Maudud (1937), Hasan Al-Banna (1939), Hafiz Al-Rahman (1942), Muhammd Hamidullah (1944), Anwar Qureshi (1946), Naiem Siddiqi (1948) and Mohammad Yousuf Al-Dean (1950)" (p.14). |
| The second phase: The emergence and establishment of interest free banks (1963-1976). | The first attempt to establish an interest free bank was made by in the rural area of Pakistan in 1950s and then on 25th July 1963.Mit-Ghamar Islamic saving Bank (MGISB) establish in Egypt by el-Naggar (Chachi, 2005). Researchers consider Mit-Ghamar as the first interest free bank in Islamic society. After the establishment of Mit-Ghamar Bank, many studies on the emergence of interest free finance was done and different conferences was done by institutional level. Among them:<br>▪ The Financial Ministers of the Islamic Countries (OIC) conference held in Karachi in 1970.<br>▪ The first International Conference on Islamic Economics in Makkah in 1976.<br>▪ The International Economics Conference in London in 1977, and an Egyptian study in 1972.<br>▪ In 1971, Nasser Social Bank was established in Egypt, in 1974, OIC`s finance Ministers held a convention on the establishment of Islamic Development Bank (IDB).<br>▪ In 1975, the Dubai Islamic Bank was established as a joint stock company. |
| The third phase: The spread of Islamic finance (1977 to present). | In this phase, several Islamic banking and financial institutions are established. International Association of Islamic Banking in 1977, International Institute of Islamic Banking and Islamic Economic in 1981, the Supreme Supervisory Commission on Fatwa and Sharia in 1983, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOFIFI) in 1990, the Islamic Financial Service Board (IFSB) in 2002, and other are established(Alharabi,2015). |

In general, in the current stage, Islamic financial institutions are rapidly growing after 2000. One of the main reason for this rapid growth is the introduction of new financial products like *Sukuk*, commodity *murabaha* and Islamic derivative (Nagaoka, 2012).

Khan (1994) stated that, Islamic Economics is applicable through Islamic banks, *zakah, takaful, waqf* and *hisabah.* Interest free financial services are offered by institutions such as Islamic commercial bank, Islamic capital markets (Equity fund and Sukuk) and Islamic Insurance (Tkaful) (Hayat and Malik, 2014). According to Abedifar et al. (2015), currently Islamic financial services are offered through Islamic banking, Islamic capital market (mutual fund and sukuk) and Insurance (*Takaful*). In addition to the above mentioned Islamic financial institutions, interest free microfinance also emerged. Institute of Islamic Banking and Insurance (IIBI) argued that, Interest free microfinance is one of the aspirant for application of Islamic finance.

### 2.3.3 Principles of Islamic Finance

Every activity in Islam weather it is *Ibadah* or *Muammalet*, should be compliant with sharia. Muslim scholars derived principles of Islamic finance from *Quran* and *Sunna.* The main principles are prohibition of interest and permission of trade, avoiding *Gaharar*, avoiding gambling and game of Chance, profit and loss sharing, requirement of *Zakat* and avoiding participation in prohibited investment (Uddin,2015; Ökte, 2010; Ayub, 2009). Financial services and products to be Islamic, they should possess the above principles.

#### 2.3.3.1 Prohibition of 'Riba' and Permission of Trade

Linguistically, the Arabic word "*riba*" means to increase, to grow, to multiply and to climb (Iqbal, 2006; Ahmed and Hassan, 2007 and Siddiqi, 2004). Jurisprudentially, the word *riba* means increase in particular things, either conditional excess for delay of payment or the selling of an item for another of the same type on spot, but in excess (Al-Fawzan,2005). The English meaning of the word *riba* is broader than the term usury (Interest above the legal or social accepted rate) (Visser, and Macintosh, 1998) and interest (The excess of money paid by borrower to the lender above the principal) (Siddiqi, 2004).

According to Homer and Sylla (2005), credit is ancient as human being itself. In the ancient era, credit was without interest for friends and neighbors. On the other hand, for productive purpose credit was interest based. In general, the concept of interest did exist in ancient time. Even though the three Abrahamic beliefs, i.e. Judaism, Christianity and Islam, all of which had strictly prohibited interest in their original teaching. Only Muslims are trying to observe their religious principle regarding to the prohibition of interest (Meera, 2004). In the Medieval and renaissance Europe, usury was strictly prohibited by Church and State. Homer and Sylla (2005) stated that:

> From this time for 300 years the attack against usury was pressed intermittently by both Church and State. In 850 lay usurers were excommunicated by the Synod of Pavia. However, it was not until the eleventh century, when European learning and trade revived, that the Church`s doctrine on usury was examined in detail by scholars and the prohibitions were spelled out by Church authorities. Usury was then declared to be even a form of robbery: a sign against the Seventh Commandment (p. 68).

However, in the Medieval and renaissance Europe usury was prohibited and interest allowed. They defined interest as a compensation for creditor for the loss that will occur through lending. Furthermore in 1950, the Roman Catholic Pope Pius approved the current interest based banking system (Homer and Sylla, 2005). The prohibition of *riba* is one of the distinctive principles of Islamic finance and all Islamic school of thought agreed on the prohibition of riba (Iqbql, 2006, Razi, 2008). The prohibition of *riba* is explicitly stated in Quran and Sunnah without doubt. Among several verses clearly shows the prohibition of riba; Allah, exalted be He, says:

> Those who devour usury will not stand except as stands on whom Evil One by his touch hath driven to madness. That is because they say: "Trade is like usury," but Allah hath **permitted trade and forbidden usury**. Those who, after receiving direction from their Lord, desist, shall be pardoned for the past; their case is for Allah (to judge); but those who repeat (to offence) are companions of the fire: they will abide therein (forever). Allah will deprive usury of all blessing, but will give increase deeds of charity: for He loveth not creatures ungrateful and wicked (Surah Al Baqarah 2:275-6).

In this versus Allah decrees that trade is permitted and *riba* is forbidden. And He also warns the severest threat to those who returned to dealing with *riba* after knowing that Allah has forbidden it, they will be the inhabitant of fire eternally. In addition to these, Allah wipes out the blessing of the money that earned from dealing in riba (Al-Fawzan, 2005). In addition to the abovementioned versus, in *Al-Baqarah* 2:278-9, *Al-Imran* 3:130, *An-Nisa* 4:161 and *Al-Rum* 30:39 clearly stated that *riba* is prohibited, unlawful appropriation of others property and Muslims are asked to take only the principal in the lending money. The prohibition of *riba* also clearly stated in prophet's *Sunnah*. *Riba* is one of the destructive Sins stated in Sunnah. These are attributing a partner to Allah, practice of magic, killing of life without just cause based on Islamic law, **eat up of riba**, eat up of orphan's wealth (Bukhari 4:28). The Holy prophet cursed the one who take interest and the one who pays it. He said "Allah`s Messenger (may peace be upon him) cursed the accepter of interest and its payer, and one who records it, and the two witnesses, and He said: they are all equal" (Muslim Book 10 No: 3881).

Muslim Jurists classified *riba* in to two types: *Riban-Nasiah* (Delay Usury) and *Ribal-Fadl* (Excess Usury).

***Riban-nasiah* (delay usury)**: The Arabic word '*nasiah*' means delay. This types of *riba* is two types: The first one is an increment of the debt on the insolvent person or to extend the due date by means of adding interest rate (Al-Fawzan, 2005). Regarding to extend the due date of loan, Allah, exalted be He, says: "if the debtor is in a difficulty, grant him time till it is easy for him to repay. But if ye remit it by way of charity, that is best for you if you only knew" (Surah Al Baqarah 2:280). In this verse indicates that, if the debtor is unable to pay with in due date, it is not allowed for creditor to raise the debt; rather the creditor may give grace period for debtor or cancel the debt by way of charity. The second types of delay usury are existing in credit transactions, when two goods of the same type are exchanged but one or both parties delay the date of delivery (Razi, 2008). The messenger of Allah also said exchanging of the same items should be on spot. He said: "There is no riba in hand-to-hand (Spot) transaction" (Muslim).

***Ribal-fadl* (excess usury):** *Ribal-Fadl* refers to the exchanging of an item with another similar item but in excess (Al-Fawzan, 2001). Concerning to this types of *riba*, the holy prophet prohibited exchanging one of the six items more than others in weights or measures. The Holy prophet said: "Gold is to be paid for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, and salt for salt, like for like and equal for equal, and payment is to be made hand to hand" (Related by Imam Ahmad and Imam Muslim). The above Hadith signifies that, exchanging the same items should be like for like, equal to equal and the payment made on spot, otherwise the transaction is prohibited. According to Al-Fawzan (2005), the rest of six items mentioned the above Hadith, the same ruling applied.

Regarding to the reason behind in prohibition of *riba*, Al-Fawzan (2005) stated that the wisdom behind prohibiting dealing in *riba* are it is consuming other`s wealth irrationally, it prevents mutual support among peoples, and it affects gains, trade and professions. Razi (2008) also stated the reason why Islam prohibited *riba*? He replied that *riba* creates a people and values totally different from Islamic doctrines, it is eating people's money unjustly, to protect the wealth of people to taken by usurers, it creates selfishness environment and Islam promote charity instead of *riba*. Furthermore, Siddiqi (2004) Stated five reasons inferred from Quran for the prohibition of *riba*. These reasons are *riba* harms society, it means inappropriate use of other's property, its extreme effect is negative economic growth, it weakens human nature and it is unreasonable.

#### 2.3.3.2 Avoiding *Gaharar*

The second principle of Islamic finance is prohibition of *gaharar*. Glossary of Financial Terms define gaharar as follows:

> "Gharar literally means uncertainty, hazard, chance or risk. Technically, sale of a thing which is not present at hand; or the sale of a thing whose consequence or outcome is not known; or a sale involving risk or hazard in which one does not know whether it will come to be or not, such as fish in water or a bird in the air. It is an exchange in which one or more parties stand to be deceived through ignorance of an essential element of the exchange. Thus, is refers to an element of absolute or excessive uncertainty in any business contract. The *Hanafi* School of Islamic jurisprudence defined *gharar* as 'that whose consequences are hidden.' *The Shafi* school defined *gharar* as 'that whose nature and consequence are hidden' or 'that which admits two possibilities, with the less desirable one being more likely.' The *Hanbali* school defined it as 'that whose consequences are unknown' or 'that which is undeliverable, whether it exists or not. (NA)

Scholars classified *gharar* in to two types: *Gharar al-Kathir* (excessive *gharar*) and *Ghararal Qalil* (light *gharar* or nominal uncertainty). Scholars agreed that only those transactions that involve excessive *gharar* are prohibited and transactions that have involve in light gharar are tolerated and this type of uncertainty unavoidable (Ayub, 2009 and Uddin, 2015). There are evidences from Quran and Hadith regarding to prohibition of *gharar*. From Quran Allah, exalted be He, says: "And do not eat up your property among yourself for vanities, nor use it as bait for the judge, with intent that ye may eat up wrongfully and knowingly a little of (other) people's property" (Al-Baqarah 2:188). In Hadith, also the Holy Prophet prohibited *gharar* in distinct types of selling. The prophet (PBUH) said to Hakim ibn Hizam: "Do not sell what you do not have (or possess") *(*Related by Ibn Majah and At-Tirmidhi).

Ayub (2007) stated that to be far away from uncertainty, Islamic law rejects the right to sell in the following three conditions:

1. When thing which are intended for transaction do not exist,
2. Things which exist but which are not in the ownership of the seller or the availability of the item is not known, and
3. Things which are traded based on undefined transfer of item and payment (p.60)

*Gharar* can exist in diverse ways, Ayub (2007) listed the following as an example of *gharar*. Selling of an item that the seller is unable to deliver the item to the buyer, selling of unspecified item with undetermined price, selling an item without deciding on price, enter in to a contract by conditioning unknown event, selling an item based on wrong explanation, and selling an item without permitting for the buyer to observe the item.

#### 2.3.3.3 Avoiding *Maisir and Qimar* (Game of Chance)

*Maisir* and *qimar*are an Arabic word and they can be use identically (Ayub, 2009). Glossary of Financial Terms defined the word *qimar* literally refers to gambling. Technically, the arrangement is, the ownership of a property is depending on the uncertain event. This implies that there is a specific gain for one party and a specific loss for another party. No one know which party will gain and which party will loss. *Maisir* also defined as a game of chance or gambling, attempting to get money easily without having equal deliberation. It is a forbidden activity, a zero-sum game just moving wealth from one person to another one without generating new wealth.

The term *maisir* and the word *qimar* are discussed Hadith (Ayub, 2009). Evidence from the Holy Quran regarding to *gambling*:" They ask thee to gamble. Say: 'In them is great sin, and some profit, for them; but the sin is greater than the profit'…." (Al-Baqarah 2:219). In Quran Chapter five Al- Ma'idah verses 90 and 91, gambling stated as the action of Satan and hindrance from the remembrance of Allah respectively.

Ayub (2009) states that:

> *Maisir* and *Qimar* are involved in a number of financial transactions and bank schemes/products which Islamic banks should avoid. Conventional insurance is not Sharia compliant due to the involvement of *Riba* and *Maisir*. Government and private sector corporations mobilize resource based on lottery and draws, which come under the banner of gambling and are, therefore, prohibited. Present future and options contract that are settled through price differences only are covered under gambling (p.62).

#### 2.3.3.4 Profit and Loss Sharing (PLS)

PLS is a principle of Islamic finance to conform to the ban of interest. It refers to a sharing of risks and profit between partners engaged in a financial transaction. PLS is one of the main futures of Islamic finance that distinguished it from interest based conventional banking (Mirahkhor and Zaidi, 2007). Institute of Islamic Banking and Insurance (IIBI) states that Islamic financial system uses the principles of participation in a contract backed by real asset, using the money at risk on profit-and-loss sharing basis. Hussain, Shahmoradi and Turk (2016) noted that, the principles of profit and loss sharing is the core of Islamic finance, guaranteeing that increase in capital should come from productive activities. Profit and loss sharing principle applied through Mudarabah and Musharakah mode of financing. Such mode of financing allows the financier to have share the project through partnership with potential entrepreneur who does not have financial resource to start his/her business (Kayed, 2012).

#### 2.3.3.5 Paying and Collecting *Zakah* (Alms)

*Zakah* is the third pillars of Islam and one of the principles of Islamic finance. The Arabic word zakat has three different meanings (Rahman, 2007). Literally, Zakah means purification or cleaning of something from dirt. The Sharia definition of Zakatel-mal is giving of a portion of surplus wealth and agricultural income of a Muslims as determined by Shariah for the use of poor and needy people (Tabash and Dahankar, 2014).

Paying of *zakah* is obligatory for every Muslim, whose wealth meets the criteria put by Sharia. One of the primary objective of Islamic financial institutions is to pay and collect *zakah*. In this regard, the National bank of Malaysia required that every Islamic financial institution must pay zakat and disclose its *zakah* policy. Sloane-White (2017) noted that: "Bank Negara requires that every Islamic banking and financial institutions in Malaysia must not only pay zakat on its asset and profit, it must make clear and disclose its zakat policy to its shareholders and depositors" (p.141).

#### 2.3.3.6 Avoiding Participation in Prohibited Investment

Keeping Islamic moral and ethical principles, such as prohibiting of harmful financial products and services is among the principles of Islamic finance (Tabash and Dahankar, 2014). In Islamic finance, there are permitted and prohibited investment areas to comply with Sharia principles. Downes (2016) listed the following investment areas as forbidden or haram.

- Conventional financial products and services,
- Tobacco business (production, distribution, giving loan for producers…)
- Gambling,
- Alcohol or pork products,
- Certain entertainment like pornography, cinemas, music….,
- Weapons or military equipment, and

- Any other immoral or unethical activates identified by sharia consultant or supervisory board.

By applying this principle, Islamic finance improve the productivity of the economic system and minimize social and economic cost of such harmful products and services (Tabash and Dahankar, 2014).

#### 2.3.4 Islamic Financial Institutions

Islamic financial services are offered through different financial institutions. For the purpose of this paper, I covered only the common Islamic financial institutions i.e. interest free banking, Islamic insurance/takaful and Islamic micro-finance.

##### 2.3.4.1 Interest-Free Banking (IFB)

Interest-free banks are deposit-taking financial institutions without paying interest on the collected deposit. Their sources of capitals are shareholders fund, saving accounts, current accounts, and investment accounts. Like conventional bank depositors, interest free bank depositors are looking for safe keeping of their moneys and suitability in using their funds (Shanmugan and Zahari, 2009).

The interest-free banking operational system defined by Al-Jarhi and Munawar (Cited in Ayub, 2009) as follows:

> An Islamic bank is deposit-taking banking institution whose scope of activities includes all currently known banking activities, excluding borrowing and lending based on interest. On the liabilities side, it mobilizes funds on the basis of a Mudarabah or Wakalah (agency) contract. It can also accept demand deposits, which are treated as interest-free loans from the clients to the bank and which are guaranteed. On the assets side, it advances funds on a profit-and-loss sharing or a debt-creating basis, in accordance with the principles of the Shariah. It plays the role of an investment manager for the owners of time deposits, usually called investment deposits. In addition, equity holding as well as commodity and asset trading constitute an integral part of Islamic banking operations. An Islamic bank shares its net earnings with its depositors in a way that depends on the size and maturity of each deposit. Depositors must be informed beforehand of the formula used for sharing the net earnings with the bank." (P.187)

Khan (1994), described that, interest free banks implement their financial products and services through:

- Equity participation (*musharakah* and *mudarabah*),
- Leasing *(ijarah*),
- Lease-purchase *(ijarah wa iqtina*),

- o Cost-plus financing (*bay` murabahah*), and
- o Rent sharing (p.80)

Ayub (2009) also states the following mode of interest free financing: *musharakah* (equity participation), *Mudarabah* (profit-sharing and loss-absorbing), Leasing *(ijarah*) and trading tangible goods or sale contract with deferred payment (*Bai`Muajjal*) or with deferred delivery of goods (*Bai`Salam and Istisna`a*). Interest free banks offere many financial products and services. This products and services are classified in to distinct groups based on their types. Among these classifications, we will summarize the classifications of Obaidullah (2005), Ayub (2009) and Laldin (2008) in the following table.

Table 2.4 Classifications of IFB Products and Services

| **Obaidullah's (2005) Classification** | | |
|---|---|---|
| No. | Category | Products and services under category |
| 1 | Deposits Services | Current deposit, Saving deposit, Investment deposits |
| 2 | Retail/Consumer Banking | Housing and Property finance, Hire Purchase, Share Financing, working capital Financing, Credit and Charge card. |
| 3 | Corporate Banking/Trade Finance | Project Financing, Letter of Credit, Venture Capital, Financing Syndication, Revolving Financing, Short-term Cash Advance, Working Capital Finance, Letter of Guarantee, Leasing, Export/Import finance, Construction, Bill Discounting and Underwriting and Advisory service. |
| 4 | Treasury/Money Market Investment Products | Sell and buy-back agreement, Islamic Bond, Government Investment Issues |
| 5 | Other Products and Services | Stock-Broking Service, Fund Transfer (Domestic and Foreign), Safe-keeping and Collection (Negatable Instruments), Factoring, Administration of Property, hiring of storage Boxes, Demand Draft, Traveler's Cheques, ATM services, Standing Instruments, Telebanking. |
| **Ayub's (2009) Classification** | | |
| 1 | Deposit/Fund Mobilization | Current deposit, saving deposit, differ types of Investment deposits, Individual portfolios and Liquidity generation. |
| 2 | Trade finance, | Project finance, working capital finance, Export finance-preshipment, import finance, Cash finance, Export financing- Post Shipment (bill discounting), letter of credit, letter of guarantee. |
| 3 | Corporate finance | Production finance for input and pesticides, Tube wells, tractors, trailers, farm machinery and transport (including fishing boats), Plough cattle, milk cattle and other livestock; dairy and poultry, Storage and other farm construction (sheds for animals, fencing, etc.) Diminishing Musharakah or rent-sharing Land development, Orchards, nurseries, forestry. |
| 4 | Agriculture, Forestry and Fisheries | Money market- interbank Liquidity management, Fund management, Trading in Sukuk, Stocks and Forex operation. |
| 5 | Treasury | Consumer durables, Automobiles, housing finance and Providing cash for personal needs. |
| **Laldin's (2008) Classification** | | |
| 1 | Deposits | Current deposit, Saving deposit, Investment deposits |
| 2 | Financing | Benevolent loan, Bridge finance, Cash line facility, Computer financing, Contract financing, Education financing, Equipment financing, Factoring financing, Fixed asset financing, Hire purchase, House financing, Land financing, Project financing and others. |

| | | |
|---|---|---|
| 3 | Treasury/Money market Investment | Government Investment issue, Islamic treasury bills, Commercial papers, Negatable debt certificate, sell and buy back agreement, Forex exchange. |
| 4 | Trade Financing | Accepted bills, Bank guarantee, Export credit refinancing, Letter of credit, Shipping Guarantee, Trust receipt. |
| 5 | Card Services | Charge card, Credit card, Debt card |
| 6 | Banking Service | Stock broking service, Fund transfer, Travelers` cheques, Cashiers` order, Demand draft, Standing instruction, ATM services, Telebanking. |

The common Interest-free banking products and services are briefly explained below.

- **Deposit Services**

Interest free banking provides the following deposit services.

**Current Account/*Amanah***: In this type of deposit account, the account holder accumulates his money in the bank only for the sake of safe keeping purpose. There is no return in this account. The bank guaranteed the principal amount for depositor (Hussian, Shahmoradi and Turk: 2015). The bank can use this fund at its own risk. Any returns and risk rising from the investment of this fund completely transferred to the bank (Ahmad, Awan, & Malik, 2011).

**Saving Account/*wadia***: This type of deposit account is used by the account holder for safekeeping purpose and to receive a return. The major features of this account are that the depositor save his money for safekeeping purpose, the bank request the depositor to use the money, the bank claim ownership over all returns gained from the use of this fund, reward the depositor by giving a portion of the profit: it is absolute discretion, the bank guarantee the withdrawal of the money at any time (Visser, 2013).

**Saving Account/*Mudarabah***: Usmani (2004) defined *mudarabah* as followes:

*"**Mudarabah*** is a special kind of partnership where one partner gives money to another for investing it in commercial enterprise. The investment comes from the first partner who is called ***rabb-ul-mal***, while the management and work is an exclusive responsibility of the other, who is called ***mudarib"*** (P: 31).

*Mudarabah* is one of the alternative saving account that the bank invests the money by requesting or by representing the depositor as *mudarib* and the customer who deposit his money at the bank act as *rabb-ul-mal.* If there any return on the investment, the bank and the depositor will divided based on the agreed ratio (Jelil and Rahman, 2010).

**Investment Account /*Mudarabah***: Investment deposit is the main deposit product of interest free bank. This product is based on *Mudarabah* and it is also called profit-and-loss sharing or participatory deposit. There are several types of investment deposit: The first one is General Investment Deposit/ *Mudharabah mutlaqah*: This type of investment deposit implemented by IFB by establishing investment pool. The pool consists of different deposits at different maturities. The funds are not tied to a single investment, instead it utilized in different investment. Returns are calculated and disseminated at the end of the accounting period. The second type is Special Investment Deposit/ *Mudharabah muqayyadah*: It is like general Investment Deposit, except in this case the bank requests the depositor minimum amount and the mode of investment and profit sharing ratio is particularly negotiable. The third type is Limited and Unlimited Period Investment Deposits: In case of limited period of investment, deposits are accepted for a definite period. Contact terminates at the end of specified period. The unlimited period of investment deposit, period is not specified and withdrawal or additional deposit is not permitted in this account. The customer can open additional account. Profit is calculated at the end of accounting period for both types. (Obaidullah, 2005).

- ❖ **Financing Products (equity-based)**

Interests free banking financing practice are currently shows that it is ready to employ reasonable modes of finance through *Musharakah* and *Mudarabah,* whether to finance trade, industry or a budget deficit through domestic or foreign source. *Musharakah* and *Mudarabah* can be exercised for short, medium and long-term project financing, import financing, pre-shipment export financing, working capital financing and for financing all single transactions (Ayub,2007). *Mudarabah* (Trustee project finance) and *Musharakah* (Joint Venture finance). The former refers to a mixture of entrepreneurship and capital while the latter refers to a partnership in entrepreneurship and capital. There is also a new concept of declining/diminishing *musharakah* leading to whole ownership of asset or project by the customer-entrepreneurship (Shaikh, 2010).

**Trustee Partnership (*Mudarabah*)**: Trustee partnership based on *mudarabah* is a mode of financing through which the bank (*rabb-ul-mal*) provide finance for an investment to the customer (*mudarib*) Usmani (2004). In this partnership, the bank is the possessor of capital and the customer-entrepreneur is accountable for operating the business and to provide every necessary materials and manpower. Profit is shared based on their agreement and losses if any, are completely absorbed by the capital provider (the bank). There are two types of *mudarabah*. The first one is restricted *mudarabah (mudarabah al muqayydah)*- the bank or the customer may specify a single investment type. The second type is unrestricted *mudarabah (mudarabah al-mutlaqah)*; the customer may invest the capital in any types of business he thinks suitable (Hassan, & Bello, 2014).

**Joint Venture *(Musharakah*)**: *Musharakah* is an Arabic word it means sharing. The concept of *musharakah* in trade and investment refers to a types of investment partnership in which all partners share the project's profit based on a stated ratio but losses are shared in percentage to the amount of capital invested. All parties are entitled to participate in the management of the project (Shanmugam and Zahri, 2009).

**Combination of *Mudarabah-Musharakah***: *Mudarabah and Musharakah* can be combined in a single investment. In this mode of financing the customer (*Mudarib*) contribute some money in the investment with the money of the bank (*rabbul-al-mal*). The customer will get more profit by acting as *mudarib* (responsible for the management of the business) and as a partner (*sahrik*). In such case the sleeping partner in *musharakah* can get only his share of investment (Rahman, 2010).

**Diminishing *Musharakah***: The new form of *musharekah* developed in the near past is diminishing *Musharakah.* In this mode of financing, the financier (the bank) and his customer share either in the joint possession of an assets or an equipment, or a joint business enterprise. The part of the bank is further split in to several units and it is assumed that the customer will acquire unites of the shares of the bank one by one periodically. The customer will continue in buying of the banks share till he becomes a sole owner of the property or equipment. This mode of financing usually used for house financing and it can also apply to purchase a taxi for offering transport service and to start a business of ready-made garments (Usmani, 2004).

- **Financing Products (debt-based)**

The above-mentioned equity based financing products are more exposed external shocks compared to conventional banking financing products. However, the interest free banking equity based products are more superior to conventional banking products from the perspective of ethics, fairness and social justice. Currently, interest free banks expand their financing products by implementing debt-based mode of financings, such as *murabahah, bai-bithaman-ajil (BBA), ijara, salam, istisna, istijrar, qard-al-hasan,bai-al-dayan, bai-al-einah, and tawarruq*. These debt-based interest free bank financing products are categorized in to three groups, such as, generally acceped and most popular (*murabahah, bai-bithaman-ajil (BBA)* and *ijara*), non-controversial propucts (*salam*, *istisna*, *istijrar* and *qard-al-hasan*) and controversial products (*bai-al-dayan*, *bai-al-einah*, and *tawarruq*) (Obaidullah, 2005).

***Bai Bithaman Ajil*/ABA (Deferred Payment Facility)**: ABA is a sale of goods on the bases of deferred-payment. The bank purchases a good and sell it to the client at cost-plus profit margin fixed by both parties. The bank is not obligatory to release the price and profit margin. Payment can be made at instalment base i.e. monthly, quarterly, or semiannually (Shanmugam and Zahri, 2009).

***Murabahah* (Cost-Plus Sale)**: *Murabahah* is an agreement between the bank and the customer, the customer agrees that the bank deliver him a definite good by adding a certain profit on the cost. The core element of *murabahah* is that the seller (the bank) reveals the actual cost he has incurred in buying of the good and the profit him thereon. The profit may be in lump sum or based on percentage. The payment may be at spot or a later date agreed in the future (Usmani, 2004).

***Ijarah* (Leasing)**: *Ijarah* is an Arabic term which means to give something on rent. In Islamic law, the term is used for two situations such as hiring human services and hiring usufructs of property (Rahman, 2010). *Ijarah* (Leasing) denotes to an agreement in which a bank (the lessor) rents equipment, a house or other properties to a customer (the lessee) at agreed rental fee for a specific period. Possession of the property remains under the lessor (Shanmugam and Zahri, 2009). Interest free banks can implement this mode of financing by two arrangements. The first one is the bank purchase the asset needed by its customer and after possessing the asset lease out it for its customer. The second arrangement is that the bank appoint the customer as its agent. The customer purchases the asset on behalf of the bank and when the asset delivered to him, he is responsible to meet his requirement as a lessee (Obaidullah, 2005). There are two types of *Ijarah*: *Al-ijara thuman al-bai* (leasing and subsequent purchase) and *Ijarah muntahia bittamlee*k (buying back leasing) (Shanmugam and Zahri, 2009).

***Salam* (Deferred Delivery Sale)**: Salam defined by Muslim scholars as: “A contract according to which the price of a clearly defined item is paid in advance at the place of concluding the contract, and the sold item is to be received later” (Al-Fawzan, 2005:59). In a *salam* contract, a trader in need of short-term finances sells commodity to the bank on a deferred delivery basis. It accepts full price of the commodity on the spot that helps its financing needs at present-day. At a pre-agreed upcoming date, it transfers the commodity to the bank. The bank sells the commodity in the market at the current price.

***Istisna* (Manufacture-Sale)**: *Istisna* is an agreement between manufacturer and the purchaser, when the later order the former to manufacture a specified item, with the raw material to be provide by the manufacturer. The agreement of both parties and description of the item must be prearranged. *Istisna* can be used as a mode of financing for house building, project financing and Build, Own and Operate (BOO)/Build, Own and Transfer (BOT) (Rahman,2010). *Istisna* allows financial intermediaries like IFB to involve in the contract of *istisna* with manufacture or contractor on behalf of a third party under *parallel istisna* agreement. The difference between of the price accepted from his customer and the price paid to manufacturer create profit for the bank (Iqbal, & Mirakhor, 2011).

***Istijrar* (Recurring Sale)**: *Istijrar* is a buying of different amounts of a given product from a single seller over a period of time. This means the seller delivers the whole amount of product acquired in installment. The repetition of buying products from a single seller may results in deferred price to the feature or average price dominant in the market based on normal price (Kettell, 2011).

***Qard* (Benvolent Loan)**: *Qard* (Benvolent Loan) refers to a free, or benevolent agreement in which borrower is required to repay only the amount borrowed with no profit (mark-up) to the lender (Shanmugam and Zahri, 2009).

***Bai-al-Einah* (Repurchase)**: Bank Negara Malaysia defined *Bai-al-Einah* as:*"Bai-al-Einah* refers to an arrangement that involves sale of an asset to the purchaser on a differed basis and subsequent purchase of the asset at cash price lower than the differed sale price or vice versa, and which complies with the specific requirement of *bai-al-einah*" (BNM/RH/CP O28-2:4).The bank acquisitions a commodity from its customers and on a spot price and sell it back to the customer at a cost-plus price and on a deferred basis (Nursyamsiah, & Kayadibi, 2012).

***Bai-al-Dayn* (Sale of Debt)**: Seman (2002) defined *Bai-al-Dayn* as: "a sale of payable right arising normally from a transaction, services, and loan to either the debtor himself, or any third party" (P:99). There are two circumstances where *Bai-al-dayn* can exist. The first one is *Bai-al-dayn* to the debtor and the second is *Bai-al-bayn* to the third party. In both circumstances debt could be sold in credit or in cash. In the first case, the debt is sold in credit (selling debt with debt) which is prohibited in the agreement of all Muslim scholars. When sales made in cash, majority Muslim scholars permitted selling of debt to the debtor in cash. Regarding to selling of debts to the third party with cashes, majority Muslim scholars prohibited (Seman, 2002).

***Tawarruq* (Tripartie Sale)**: Obaidullah (2005) stated that, *tawarruq* is one of the IFB product that Muslim scholars are dispute on it and the mainstream scholars are permitted it. He defined it as: *"Tawarruq* become a source of fund by combining two separate sale and purchase transactions. An individual in need of funds purchases a commodity on deferred payment basis from the seller and then sells the same in market to realize cash." (PP: 109)

- **Fee Based Products**

Interest free banks offer a full range fee based banking services which are offered by conventional banks. Fee-based products offered by interest free bakes are letter of credit, letter of guaranty, safe keeping of negotiable instrument, domestic and external money transfer, hiring strong boxes and administration of property (Obaidullah, 2005).

**Forms of Islamic Banks**: Currently, throughout the world, Islamic banks are established in different forms or models. According to Sole (2007) and Abedifar et al (2015), there are three models of Islamic banks. These three models of Islamic banks are summarized in the table below.

Table 2.5 Models of Islamic Banks

| No. | Models | Definition |
|---|---|---|
| 1 | Full-fledged Islamic Banking | A bank established based on sharia principles with independent infrastructure and offer full-range of sharia compliant products and services. |
| 2 | Islamic Window | A model of Islamic banking, conventional banks offer sharia compliant financial products and services by using existing infrastructure including branches and staffs. |
| 3 | Islamic Subsidiaries Banks | A dedicated governance of Islamic bank like full-fledged, established by conventional banks as subsidiaries. It may also share infrastructures from conventional banks. |

#### 2.3.4.2 Islamic Insurance/Takaful

The majority sharia scholars agreed that the conventional insurance practice is against Islamic financial principles (Obaidullah, 2005). As stated by Rahman (1974), there are four unlawful elements in the contract of insurance i.e. interest (*riba*), gambling (*qimar*), risk probability (*garar*) and uncertainty (*Juhala*). Because of the above mentioned unlawful elements of insurance, Muslim societies need an alternative for conventional insurance. The Islamic alternative of insurance is known as *Takaful* or Islamic insurance. The term Takaful is originated from the Arabic word Kafala, which denotes to warranty; to help; to take care of one's needs (Alhabashi and Razak, 2010). IFSB (2007) define Takaful or Islamic insurance as follows.

> Takaful, which means "guaranteeing each other" or "mutual guarantee" or "solidarity", is based on the concept of cooperation between members or Takaful holders/participants who contribute a certain amount of money in the form of a tabarru`(donation) to common pool, which will be used to provide indemnification against losses arising from specific categories of risks. PP.10

The origin of Takaful is dated back to the era of pre-Islamic period. Alhabashi and Razak (2010) stated the following ancient Arab practice.

> If a member of the tribe committed murder, for instance, it could lead to one of two consequences. Either a tribal war broke out to avenge the death of the tribal member, or settlement was reached by paying 'blood money'. The money that was used to compensate the loss of life came from the tribal fund which was collected from donations by the members. Once the donation was collected, no refund was allowed. The fund was used mainly to settle compensation in tribal disputes. It could also be collected when a dispute had occurred or whenever the fund was depleted. This practice is known as al-ʿāqilah. This cooperation on the part of the whole group and community to mutually share the burden of any of its members reflects the spirit of mutuality in takāful. The payment of blood

> money was an obvious example of mutual insurance, wherein the whole community stood guarantee against the loss to any of its members. PP.278

The modern practice of Islamic insurance was started in in the late 1970s. The first Islamic insurance company was established in Sudan in 1979. Following the success of this company, the practice of Takaful expands throughout the Muslim and Non-Muslim countries (Hussain and Pasha, 2011).

According to Alhabashi and Abdul Razak (2010), the followings are the main principles of Islamic insurance.

- Policy holders cooperate among themselves for their common good;
- All policy holders pay his subscription to help those that needed assistance;
- Losses and liabilities shared based on the community pooling system;
- Uncertainty is eliminated in respect of subscription and compensation; and
- Advantage is not derived at the cost of others. PP.281

Types of Takaful Models: According to Obaidullah (2005); Ayub (2007); Swartz & Coetzer (2010); Akhter (2010); Htay, & Zaharin (2012) and Pasha, & Hussain (2013), there are three models of takaful. The three common modes of Islamic insurance are presented in the following table.

Table 2.6 Models of Takaful

| No. | Models of Takaful | Meaning |
|---|---|---|
| 1 | Tabarru Model | A non-profit model of Takaful, member’s donation (Tabarru) to the Takful fund, which is used to extend financial assistance to any member based on their agreement. |
| 2 | Mudaraba Model | Members and workers go into in a mudarabah agreement for corporative sharing of losses of members and profit if any Profit is disseminated on a jointly agreed ratio. |
| 3 | Wakala Model | In case of wakalah model, the takaful manipulator acts as a representative for the members and acquires a payment in the form of a fixed ratio. |

### 2.3.4.3 Islamic Microfinance

Micro finance is a type of financial institution aimed to provision of financial services to the poor and low-income people whose financial standing excludes from the formal financial system (Obaidullah, 2008). Modern microfinance was started in Bangladesh in 1976 by Professor Muhammad Yunus. Micro finance is a poverty alleviation program by offering financial services for poor society. However, conventional microfinance services criticized for higher interest rate on the loan provided to poverty alleviation purpose. The interest rate asked by conventional micro finances is higher than the standard loan in developed worlds (Helms & Reille, 2004). Conventional microfinance services don not attract the majority Muslim population around the world. Interest is the main reason hindering Muslims from accessing conventional microfinance. It is against the principles of Islamic finance (Dhaoui, 2015). Regarding to the need of Islamic microfinance, Obaidullah (2008) stated that:

> Islamic societies are characterized by high and rising levels of poverty and financial exclusion. Financial exclusion is aggravated by failure on the part of conventional microfinance programs to give due importance to the religious sensitivities of Muslims. For poverty alleviation efforts to succeed in these societies, there is need for an appropriate model that is rooted in Islam and conforms to beliefs, cultures of the Muslim clients (NA)

By considering the role of microfinance in poverty alleviation and non-compliant with sharia principles, the Islamic model of microfinance project started in Sudan in 1980s (Mollah and Uddin, 2013). Islamic microfinance is a financial institution that provides sharia compliant financial services for poor to alleviate poverty (Dhaoui, 2015).

Products of Islamic Microfinance Institutions (IMFIs): Islamic microfinance institutions are offering different sharia compliant financial products. In the following table, the researcher summarized the classification of Obaidullah (2008).

Table 2.7 Products of Islamic Microfinance

| | |
|---|---|
| Non-profit models of Islamic Microfinance Products | |
| Zakah | By collecting portion of surplus wealth and agricultural income of the Muslims that determined by Shariah for the use of poor and needy people those are described in Quran. |
| Awqaf | By receiving from donors, a certain non-perishable asset and protecting it so that aids constantly flow to a definite group of beneficiaries or society. |
| Qard Hasan | A loan collected from a lender without any return on the principal. This used as a method saving mobilization and financing. |
| Profit-Based Islamic Microfinance Products | |
| Micro-Saving | • Wadia: Saving Account, Qard Hasan: benevolent loan and Mudarabah: Revenue based Saving account |
| Micro-Credit | • Bai-Muajjal-Murabaha: Differed payment sale<br>• Ijara: Leasing of a Physical asset<br>• Bai-Salam: Differed delivery contract<br>• Bai-Istisna: Contract of Manufacture<br>• Bai- Istijrar: The seller deliveries in instalment base |
| Micro-Equity | ▪ Mudarabah: Trustee-partnership<br>▪ Musharakah: Joint venture involves partnership |

Source: Obaidullah (2008)

### 2.3.5 Overview of Islamic Finance Industries

Today, Islamic finance industry expended all directions of the globe in Muslim and non-Muslim countries. According to GIFR (2016), the estimated total asset of global Islamic finance at the end of December 2016 was US$ 2.293 trillion and the growth rate was 7%. The total asset of Islamic finance has increased significantly from about US$ 5 billion in 1980s (Mohieldin.2012) to US$ 2.293 trillion in 2016. The main sectors of Islamic finance industry categorized as Islamic banks, Sukuk, Islamic funds, Takaful, Islamic microfinance and others. The share of each sectors from the total asset of Islamic finance is demonstrated in the following table.

Table 2.8 Share of Islamic Financial Institutions

| Sectors | Asset in % |
|---|---|
| Islamic Banking | 75% |
| Sukuk (Islamic Bond) | 15% |
| Islamic Funds | 4% |
| Takaful (Islamic Insurance) | 1% |
| Islamic Microfinance | 1% |
| Other | 4% |
| Total asset of Islamic finance | 100% |

Source: Global Islamic Finance Report, 2017

As stated by Islamic Financial Services Industry Stability Report (2016), the total asset held by regions in each sector is illustrated as follows. As presented in Table 2.9 below, based on the 2016 report, from the total asset of Islamic finance 39.5% (744.1 billion) and 33% (624.3 billion) held by GCC countries and MINA countries respectively. By sector, the largest portion of Islamic finance asset, 79.5 % (1496.5) came from banking sector.

Table 2.9 Islamic Finance Asset by Sectors and Region*

| | Region | | | | | |
|---|---|---|---|---|---|---|
| Sector | Asia | GCC | MINA (exc. GCC) | Sub-Saharan Africa | Others | Total |
| Islamic Banking | 209.3 | 598.8 | 607.5 | 24 | 56.9 | **1496.5** |
| Sukuk | 174.7 | 103.7 | 9.4 | 0.7 | 2.1 | **290.6** |
| Islamic Funds | 23.2 | 31.2 | 0.3 | 1.4 | 15.2 | **71.3** |
| Takaful | 5.2 | 10.4 | 7.1 | 0.5 | - | **23.2** |
| Total | **412.4** | **744.1** | **624.3** | **26.6** | **74.2** | **1,881.6** |

*US$ billion and Based on Total Asset 1.88 trillion in 2015

Source: Islamic Financial Services Industry Stability Report, 2016

In the following table, we will review the leading country on each sector of Islamic finance.

Table 2.10 Share of Global Islamic Banking Asset by Country Level

| Sector | Leading countries |
|---|---|
| Islamic Banking | Iran (37.3%), Saudi Arabia (19%), Malaysia (9.3%), UAE (8.1), Kuwait (5.9%), Qatar (5.1) and Turkey (2.9%). |
| Sukuk | Malaysia (57.6%), Indonesia (17.5%), Bahrain (5.6%), UAE (4.6%), Saudi Arabia (3.8%) and Turkey (3.1%). |
| Islamic funds | Saudi Arabia (40%), and Malaysia (28%), Jersey (8%) and United States (7%). |
| Takaful | Saudi Arabia (36.6%), Iran (33.6) &Malaysia (13.6%), |
| Islamic MFIs | Bangladesh, Sudan and Indonesia |

Source: Islamic Financial Services Industry Stability Report, 2016

### 2.3.6 Islamic Finance in Ethiopia

The history of Islamic finance in Ethiopia is categorized in to two phases.

Phase 1: The process that tried to establish full-fledge Islamic finance: Ethiopian Muslims have been asking National Bank of Ethiopia for the permission interest free finance for many years. Finally, the first interest free bank in the history of the country had been on establishment selling shares in the name of Zamzam Bank in 2008. Then, the proposed bank representatives presented their proposal for NBE officials in the meeting that the late Prime Minister Meles Zenawi attended. In that meeting, the representatives explained the need of interest free banking and its role for economic development. The late prime minister directed the NBE officials to draft a new directive that allow the establishment of interest free finance (Al-Hashimi, 2012). Therefore, a new Banking Business Proclamation, Proclamation No: 592/2008, was promulgated Banking Business. Article 22, Sub-article 2 of the Proclamation states that "The National Bank may issue directive to regulate banking businesses related **to non-interest-bearing deposit mobilization and fund utilization.**" This creates a room for establishing interest free finance. The Proclamation No: 592/2008 was the turning point the history of Islamic finance in Ethiopia.

Zamzam bank which was under establishment announced the selling of share for publics in December 2010. At that time, the minimum paid-up capital to participate in the banking industry was 75 million Ethiopian Birr. Within only four months, 137 million Ethiopian Birr was collected by from more than 6800 shareholders (Zamzam bank, 2012). After the tedious 5 years' establishment process for full-fledged Islamic finance, in 2011 NBE issued two directives which were unexpected.

The first one was in September 18, 2011, on which NBE issued a new directive named Minimum Capital Requirement for Banks: Directive No. SBB/50/2011. This directive states: "The minimum paid up capital required to obtain a banking business license shall be Birr 500 million (birr five hundred million), which shall be fully paid in cash and deposited in a bank in the name and to the account of the bank under establishment". The second directive was directive No. SBB/51/2011. This directive restricted the possibility of providing interest free finance exclusively conventional banks through interest free window. Furthermore, this proclamation dashes the dreams of more than 6800 shareholders (Ashnie, 2012).

Finally, in January 11, 2012, NBE informed the organizers of Zamzam bank by a letter dated FSB/BSD/2012 either establish a conventional bank which can offer interest free window with minimum paid up capital 500 million birr or terminating the formation of the bank. The establishment of full-fledged interest free finance terminated in May, 2012 by refunding the collected money to the shareholders (Zamzam bank, 2012).

Phase 2: The introduction of interest free window: After the termination of the establishment process of full-fledged interest free banking in Ethiopia, based on directive no. SBB/51/2011 which permitted the provision of interest free service by conventional banks, Commercial bank of Ethiopia and Oromia International bank announced the starting of interest free window services in 2013 (Alemayehu,2013). Today, totally 8 conventional banks are offering interest free window services.

In Ethiopia, there is no Islamic insurance/Takaful services and Islamic microfinance. However, according to Byrne and Anderson (2015) by the support of USAid, Mercy Corps launched the first interest free microfinance called Somali Microfinance. This microfinance has 16 branches and 6,000 customers.

### 2.3.7 The Role of Islamic Finance in Tackling of Financial Exclusion

Demirgüç-Kunt et al. (2015) stated that there are 2 billion adults in the world who have no access finance. The majority of them are from Muslim dominant countries (Mirakhor, & Iqbal, 2012). According to Global Islamic Finance Report (2017), the estimate number of Muslims in the world is 2.038 billion. Among these Muslims, not more than 20% have those who are access finance. This means, 80% of Muslims in the world have no access financial services.

One of the main reason of exclusion of Muslims from accessing finance is religious reason. The interest based conventional financial services and products do not meet the needs of Muslims as they are not compliant with sharia principles (Sain et al., 2016). To solve this religious driven financial exclusion, different scholars and financial institutions recommended the expansion of sharia compliant financial services to enhance the financial inclusions of Muslims. Demirgüç-Kunt et al. (2015) recommended the development of financial products compliant with Islamic financial principles to expanding account ownership. The fundamental principle of Islam gave a great emphasis on social justice, inclusion, and sharing of resources between the haves and the have nots (Mohieldin, 2012).

Mohieldin, et al. (2011) addressed two approaches of enhancing financial inclusion through Islamic finance. These approaches are promoting risk-sharing contracts and redistribution of wealth among societies. The instruments under the two approaches are presented in the table below.

Table 2.11 Approaches of Financial Inclusion by Islamic Finance

| Approaches | Instruments |
|---|---|
| Risk-Sharing Contracts | Islamic Banking Products and services<br>Islamic Microfinance products and services<br>Islamic Insurance/Takaful |
| Redistribution of Wealth institutions | Zakat, Sadaqa, Waqqf and Qard-al Hasan |

In general, Islamic finance provides productive financial instruments, which, if employed based on sharia principles, can reduced poverty and inequality of wealth distribution. So, to achieve these results, the expansion of Islamic financial institutions is very important. In addition to this, the expansion of Islamic financial institutions determines the financial inclusion of Muslims. The expansion of Islamic financial institutions will enhance the financial inclusion of Muslims (Mohieldin et al., 2011).

# 3 RESEARCH DESIGN AND METHODOLOGY

## 3.1 Research Design

One of the key qualities of research is related with its credibility, inclusiveness and clearness of the data, procedure employed and results. For this reason, designing methods which best suit the research question will be the main task of a researcher. Therefore, in this chapter, a detail description of methods and procedures utilized in this paper is presented. In addition to this, final copy of instruments used for data collection is also attached in the Appendix section of the thesis for further survey and reference. Since this study involves the use of participants from different age and measure at similar point in time, a cross-sectional research design which is appropriate for such study was employed.

## 3.2 Data Collection Tools

Myriads of literature indicate the value of combining qualitative and quantitative means of data collection. Bhattacharjee (2012), for instance, stated that use of qualitative means of data collection in combination with quantitative method (mixed-mode of design) helps to develop unique understanding in to a complicated social phenomenon that cannot be obtained from either type of data alone. Furthermore, Creswell (2013) also forward statement which support the above argument. He stated that mixed method of data collection is the best in providing a more comprehensive understanding of a research problem than either type of data alone. Hence, following such recommendation from literature, in this research, data were collected through combination of qualitative and quantitative method.

## 3.3 Quantitative Instruments of Data Collection

### 3.3.1 Questionnaire

As stated by Kothari (2004) collecting data through questionnaires is most widely exercised in several economic and business surveys. Survey offers a quantitative data of trends, attitudes, or opinions of a population by collecting data from the sample. Since, questionnaires are well structured, they are easier to process the data and draw comprehensive conclusions (Creswell, 2013). Therefore, in this section, a detail description of survey questionnaires utilized in this study including procedures carried out in the development process is presented.

There are different steps to develop survey questionnaires and interview questions. According to Gideon (2012) the first step in developing survey questionnaire is reviewed the existing instruments used by different researchers in the same area and the second step is a decision whether to use existing instrument as it is, modify and adapt or develop a new questionnaire. Regarding the decision whether to adopt, adapt or create new tool, different ideas are forwarded by experts. For example, Boynton, & Greenhalgh (2004) argued that, employing an existing authorized survey will save time and resources; and important to compare the result with other findings. Furthermore, Fink (2002) stated that: "Most of survey experts agree that if you are interested in measuring concepts such as political stance, religiosity, satisfaction and you are not in position to do a scientific experiment to validate the questions, you should use existing and prove questionnaires" (p. 68-69).

In line with this, an attempt was made to identify questionnaires which was employed in previous studies which have similar topic with this study. Specifically, the most similar study with my study was Warsame's PhD thesis conducted in 2009 and published the form of book in 2016. The title of his PhD thesis was "The role of Islamic finance in tackling of financial exclusion in the UK". Considering the closeness of this topic with my research title, the questionnaire employed in Warsame's (2009) was taken as main source. However, since there are contextual factors which are different from Warsame's study, some necessary modification was made from the original items. Finally, after finalizing the questionnaires, to avoid language barrier, the questionnaire was translated to Amharic language.

The final questionnaire contains 32 questions, it has been classified into five sections with specific questions for different objectives. The first section consists six questions which assess the background information of respondents like sex, age, educational level, monthly income and works status. The second sections consist of 12 questions. These questions are designed to collect data about the extent and natures of financial exclusions of Ethiopian Muslims and reasons of exclusions. Generally, the questions under this section are designed to answer the first research question of this study i.e. what is the extent and nature religious driven financial exclusion Muslims in Ethiopian? The third section of the questionnaire contains 3 questions. These questions designed to collect information for research question 2 i.e. how is the access of Ethiopian Muslims toward the existing interest free banking services offered by Conventional banks? The fourth section of the questionnaires consist 5 questions. These questions aimed to provide answer for research question 3 i.e. has the introduction of full-fledged Islamic finance in Ethiopia can significantly enhance the level of financial access to Ethiopian Muslims? The fifth and the final part of questioner has 6 questions. This part of the questionnaire was designed to assess the attitude of participants towards interest free finance and financial exclusion. This part was measured through Likert scale ranging from 1 “Strongly Disagree” to 5 “Strongly Agree”.

## 3.4 Qualitative Tools of Data Collection

### 3.4.1 Interview

To strengthen the findings of the study and inrich the data collected through questionnaire, semi-structured interview was used. Semi-structured interview is a type of interview, in which questions are prepared but the interviewer may adjust the arrangement or the question throughout the interview progress (Ary, Jacobs and Sorensen, 2010). Among the key features of semi-structured interviews are flexibility (Noonan, 2013) and the researcher can prompt and ask in detail about a given state (Kajornboon, 2005).

The key informants for interview was National Bank of Ethiopia and other commercial Banks that are offering interest free banking services by windows system. These two groups were selected based on their direct relation with the issue of financial system. National bank of Ethiopia is on the authority of issuing financial regulations and other banks are rendering interest free banking services. Therefore, interviewing personnel in this institution will render in-depth information about the topic under study.

### 3.5 Population and Sample

A population is the entire population that the researcher wants to study. In this research, Ethiopian Muslims who are living in Addis Ababa by the time of data collection were the population of the study. I selected Addis Ababa, because it constitutes people from all corners of the country. According to Ethiopian Islamic Affairs Supreme Council (EIASC), Addis Ababa has 1 million Muslims (Department of State (2005). Therefore, the sampling frame could estimate to be about 1 million.

Samples were selected using stratified sampling technique which is one of the probability sampling technique. The total population was grouped in to 10 strata based on sub-cities. From these 10 sub-cities, three sub-cities namely Addis Ketema sub-city, Kolfe Keranio sub-city and Gulele Sub-city were randomly selected. From these sub-cities areas that are believed to have substantial number of Muslim inhabitants were targeted. These areas include; Mercato (considered as the biggest market in Africa), Business centers with majority Muslim, Islamic Associations and Mosques.

Following this, using Roasoft sample calculator, a total of 384 samples were randomly selected from these three sub-cities. As evidences from literature indicated, Roasoft sample calculator is among the reliable sample size calculator/softwares (Nwachukwu, 2015). Roasoft sample calculator use population size, Margin of Error (Confidence Interval) and Confidence level to determine appropriate sample size. Accordingly, in this study, with the population size of 1 million, 95% confidence level and 5 % margin of Error (Confidence Interval), the estimated appropriate sample size become 384.

### 3.6 Data Analysis

The data collected through survey questionnaires was coded and analyzed by using Statistical Package for Social Sciences (SPSS). Descriptive and inferential statistics result that are generated through SPSS will be explored and explained. On the base of the nature of the data, appropriate statistical analysis was employed. For demographic variables and nominal data, descriptive statistic like frequency and percentage was used. For the data collected through Likert scale, inferential statistics mainly, factor analysis were employed.

To analyze semi-structured interview data, I applied the steps stated by Piercy (2004). First, I read the transcript carefully, following this, observations are developed based on evidences presented in the transcript. After this, attempt was made to identify connection between the information provided by key respondents and develop meaningful pattern. Finally, the information was organized around basic themes and analysis were made in line with the research questions.

# 4 RESULTS

## 4.1 Introduction

In this chapter, the result of the study on the Role of Interest Free Finance in tackling of financial exclusion in Ethiopia is presented. In general, the finding is presented through three main categories i.e. the respondent's demographic variables, the results of each question in the survey questionnaires and the result of the semis-structured interview. Out of the total 384 questionnaires distributed, 340 participants responded. In the process of editing to check errors and omissions, 19 questionnaires were excluded from analysis because of incomplete response. Hence, the final analysis is conducted using total of 321 responses.

## 4.2 Results of Data Collected Through Questionnaire

### 4.2.1 Respondents' Demographic Variables

Table 4.1 Respondents' Demographic Result

| Demographic Variables | Category | Frequency | Percentage |
|---|---|---|---|
| Age | 18-30 | 188 | 58.6 |
| | 31-40 | 101 | 31.5 |
| | 41-50 | 24 | 7.5 |
| | 51-60 | 7 | 2.2 |
| | Above 61 | 1 | 0.3 |
| | Total | 321 | 100.0 |
| Gender | Male | 186 | 57.9 |
| | Female | 135 | 42.1 |
| | Total | 321 | 100.0 |
| Marital Status | Married | 184 | 57.3 |
| | Single | 130 | 40.5 |
| | Divorce | 7 | 2.2 |
| | Total | 321 | 100.0 |
| Educational Level | Illiterate | 2 | .6 |
| | Primary School | 12 | 3.7 |
| | Secondary School | 63 | 19.6 |
| | Vocational Training | 25 | 7.8 |
| | Degree | 182 | 56.7 |
| | Master's Degree | 27 | 8.4 |
| | PHD | 1 | .3 |
| | Other | 9 | 2.8 |
| | Total | 321 | 100.0 |

| | | | |
|---|---|---|---|
| Employment Status | Merchant | 88 | 27.4 |
| | Student | 18 | 5.6 |
| | Employed | 164 | 51.1 |
| | Unemployed | 15 | 4.7 |
| | Other | 36 | 11.2 |
| | Total | 321 | 100.0 |
| Monthly Income | < 1500 | 22 | 6.9 |
| | 1501-3000 | 68 | 21.2 |
| | 3001-4500 | 66 | 20.6 |
| | 4501-6500 | 35 | 10.9 |
| | 6501-7500 | 40 | 12.5 |
| | 7501-10000 | 38 | 11.8 |
| | Above 10000 | 52 | 16.2 |
| | Total | 321 | 100.0 |

It is apparent from Table 4.1, the majority respondents 188 (58.6%) who participated in this study were between the age of 18 and 30. In addition to this, this table clearly shows that respondents younger than 50 represented 97.5% of the total. Regarding to gender, Table 4.1 shows that, 57.9% (186 out of 321) of the people who participated in this survey were male and the rest 41.2% (135) were female. The sample was fairly distributed between the two sexes with males slightly higher.

As demonstrated in Table 4.1, majority of participants were married (57.3%) followed by singles which account 40.5%. Divorces were constituted2.2%. Table 4.1 also shows that the highest number of respondents 182 (56.7%) qualified degree level followed secondary education 63 (19.6%). Generally, majority participants (298) of the survey were achieve above secondary educational level.

Regarding to respondent's occupation, Table 4.1 demonstrated that, 164 (51.1%) of the respondents was employee of public and private sectors while merchants and students represented 27.4% and 5.6% respectively.  Of the total participants only 4.7% were unemployed. Further, from the above table, is possible to understand that all categories of income levels were fairly represented in this survey.  From the total participants, the monthly income of 68 (21.2%) was between 1501 and 3000 Ethiopian Birr. While, 22 (6.9%) of participants have a monthly income less than 1500 Ethiopian Birr.

### 4.2.2 Respondents Access to Conventional Finance

Under this section, a detail description of respondent's access to conventional finance presented. The overall result presented under this section is expected to show the clear picture of the status and extent of financial exclusions of Ethiopian Muslims. The result is presented using descriptive statistics such as frequencies and percentages for each question. Participants access to conventional financial services such bank account, bank loan, insurance, microfinance and home financing are presented in the table below.

Table 4.2 below shows that, out of 321 people who participated in the survey, 50.8% were accessed saving account, 10.9% were accessed current account and 16.8% were accessed salary account. Totally, 286 respondents (89.1%) had an account in conventional banks. The rest 35(10.9%) respondents had no account in conventional banks. With regarding to conventional bank loan, Table 4.2 shows that, 303 (94.4%) of the total respondents who participated in this survey did not access any conventional bank loans. Only 18 (5.6%) respondents access conventional bank loans.

Table 4.2 Respondents' Access to Conventional Finance

| Financial services | Category | Frequency | Percentage |
|---|---|---|---|
| Conventional Bank Accounts | Saving Account | 163 | 50.8 |
| | Current (Checking) Account | 35 | 10.9 |
| | Time Deposit | 4 | 1.2 |
| | Special Saving Account | 30 | 9.3 |
| | Salary Account | 54 | 16.8 |
| | None | 35 | 10.9 |
| | Total | 321 | 100.0 |
| Conventional Bank Loan | Home (Mortgage) Loan | 5 | 1.6 |
| | Personal Loan | 9 | 2.8 |
| | Automobile Loan | 1 | 0.3 |
| | Business Loan | 3 | 0.9 |
| | None | 303 | 94.4 |
| | Total | 321 | 100.0 |
| Conventional Insurance | Home Insurance | 4 | 1.2 |
| | Third party vehicle Insurance | 70 | 21.8 |
| | Medical Insurance | 19 | 5.9 |
| | Other Insurance programs | 6 | 1.9 |
| | None | 222 | 69.2 |
| | Total | 321 | 100.0 |
| Conventional Microfinance | Loan services | 3 | 0.9 |
| | Saving services | 29 | 9.0 |
| | Other services | 9 | 2.8 |
| | Non | 280 | 87.2 |
| | Total | 321 | 100.0 |
| Condominium Housing | Yes | 120 | 37.4 |
| | No | 201 | 62.6 |
| | Total | 321 | 100.0 |

As shown in the above table, concerning to conventional insurance, 222 (69.2%) of respondents did not accessed conventional insurances while the remaining 30.8% of respondents were accessed diverse types of conventional insurance programs. From respondents who accessed conventional insurances, the majority (21.8%) were accessed third party automobile insurance.

As depicted in Table 4.2, while majority 280(87.2%) of the participants did not access microfinance services, it was only 41(12.7%) that indicted they accessed Micro finance products and services.

As the data shows in Table 4.2, most respondents 62.6% (201), out of 321, were not registered for home financing program. The remaining 37.4% were registered.

### 4.2.3 Purpose of Using Interest Income from Saving

Literature shows that, Ethiopian Muslims access conventional saving services by thinking to avoided interest (*riba*) by different ways. Depending on this, we presented a question to participants if they were access conventional bank saving services, for what purpose they use the interest income from their saving. The result of this question is presented in the table below.

Table 4.3 Participants' Usage to Interest Income from their Savings

| For what purpose do you use the interest from your saving? | Frequency | Percent |
|---|---|---|
| I save in special account/without interest | 191 | 66.78 |
| I give the interest to the poor people | 90 | 31.47 |
| I use the interest with principals | 5 | 1.75 |
| Total | 286 | 100.0 |

As demonstrated in the above table, the total numbers of respondents who have account in conventional banks were 286. Out of 286 respondents who have conventional bank account, 191 (66.78%) were save in special saving/deposit account. This type of account is available in all conventional banks in Ethiopia for those who do not wish to collect interest from their saving. The rest 90 (31.47%) respondents use interest based account and they donate the interest income to poor people.

### 4.2.4 Reasons for Not Accessing Conventional Finance

This section dedicated to present the detail description of respondent’s reason for not accessing conventional finance. The result presented under this section is supposed to show the obvious picture of the reason for exclusions of Ethiopian Muslims. The reasons of respondents those who did not access conventional financial services is presented in the following table.

Table 4.4 Respondents' Reason for Not Using Conventional Financial Services

| Financial services | Reason for not accessing | Frequency | Percentage |
|---|---|---|---|
| Conventional Bank Accounts | I don't want to deal with interest | 16 | 45.7 |
| | I don't need to save | 5 | 14.3 |
| | I don't have enough money to save | 13 | 37.2 |
| | Other | 1 | 2.8 |
| | Total | 35 | 100.0 |
| Conventional Bank Loan | I don't want to deal with interest | 198 | 65.3 |
| | I don't need to borrow | 85 | 28.1 |
| | I have tried but not successful | 5 | 1.7 |
| | Other | 15 | 4.9 |
| | Total | 303 | 100.0 |
| Conventional Insurance | Products are against religious principles | 128 | 57.7 |
| | I have tried but not successful | 3 | 1.3 |
| | Other Reasons | 91 | 41.0 |
| | Total | 222 | 100.0 |
| Conventional Microfinance | I don't want to deal with interest | 188 | 58.6 |
| | I don't need to borrow/save | 70 | 21.8 |
| | I have tried but not successful | 15 | 4.7 |
| | Other reasons | 7 | 2.2 |
| | Total | 280 | 100.0 |
| Condominium Housing | I don't want to deal with interest | 96 | 47.8 |
| | I have tried but not successful | 29 | 14.4 |
| | Other reasons | 76 | 37.8 |
| | Total | 201 | 100.0 |

As can be seen from the above table, from the total respondents who did not have conventional bank account, 16 (45.7%) indicated religion as factors for not having a bank account. The rest 37.2%, 14.3% and 2.8% did not have a bank account because of not having enough money, no need to save and other reasons respectively.

Pertaining to conventional bank credit, Table 4.3 presents the reasons why respondents did not use the basic conventional bank loan services. Out of 303 participants who did not use conventional loan, most of them 198 (65.3%) indicated religion as a main cause. The second main reason that was reported by 28.1% of the participant for not accessing credit was lack of interest to borrow. Additionally, as shown in the above table, 128 (57.7%) of respondents did not accessed conventional insurances due to religious reason i.e. insurance products are against religious principles. In the category of "other reasons", respondents stated lack of knowledge and lack of interest for insurance programs were the main reasons.

In connection with microfinance services, as Table 4.15 shows, most respondents 188(58.6%) who did not use micro-finance replies religion is the main factor for not accessing it. The second main reason that was reported by 70 (21.8%) participants was lack of need to borrow or save from conventional microfinance. Regarding to condominium housing, of the total 201(62.6%) respondents who were not registered in condominium housing program, their main reasons 96 (47.8%) for not registering were religious reason. In the category of other reasons, as indicated by 76 (37.8%) respondents, not having enough money, having their own house, and difficult bureaucracies in registration were also reasons for not registering.

### 4.2.5 Justification for Accessing Conventional Finance

As a principle, sharia prohibited interest based financial transactions. Some respondents were access at least one of the conventional financial services. So, it is necessary to know their justifications for accessing it. The next table summarized the justifications of respondents who were accessed one of the above mentioned conventional financial services.

Table 4.5 Respondents Justification for accessing Conventional Finance

| Respondents` Justification | Frequency | Percent |
|---|---|---|
| Unavailability of alternative Sharia compliant financial services | 128 | 48.5 |
| You do not believe they are not noncompliant with Sharia | 20 | 7.6 |
| Accessing is mandatory | 78 | 29.5 |
| Others | 38 | 14.4 |
| Total | 264 | 100.0 |

Table 4.5 shows that 128 (48.5%) of respondents said unavailability of sharia complain financial services was the main reason for using at least one conventional financial services. Of the total participants who use conventional financial services, 78 (29.5%) respondents indicated using conventional finance like third party vehicle insurance and salary account was mandatory.

### 4.2.6 Knowledge and Access toward Interest Free Banking Services

This section devoted to present the result about the knowledge and access of Ethiopian Muslims regarding to interest free banking delivered by conventional banks. The result of participant's knowledge and access to interest free banking services is presented in the below table.

It is apparent from Table 4.6 below that, 273 (85%) of participants knows about the availability of interest free banking services which is offered by conventional banks. The remaining 15% did not know about the availability of this service.

Table 4.6 Knowledge and Access of Respondents Regarding to IFB Window

| Question | Response | Frequency | Percent |
|---|---|---|---|
| Do you know IFB window services are being offered in Ethiopia by conventional banks? | No | 48 | 15.0 |
| | Yes | 273 | 85.0 |
| | Total | 321 | 100.0 |
| Types of IFB window services used | Wadiah (Saving account) | 54 | 16.8 |
| | Amanah (Current account) | 45 | 14.0 |
| | Mudharabah (Profit Sharing) | 3 | .9 |
| | Murabaha (Cost-plus sale) | 1 | .3 |
| | Not accessed | 218 | 67.9 |
| | Total | 321 | 100.0 |
| Reason for not accessing IFB services with conventional banks | Not interested as they are being offered by conventional banks | 88 | 40.36 |
| | Not interested as they are not different from conventional finances | 76 | 34.86 |
| | I have applied but was not successful | 5 | 2.30 |
| | Other reasons | 49 | 22.48 |
| | Total | 218 | 100.0 |

As Table 4.6 demonstrates, 218 (67.9%) of respondents did not access interest free banking products and services offered by conventional banks. The remaining respondents, 16.8%, 14%,0.9% and 0.3% use Wadiah (Saving Account), Amanah (Current Account), Mudarabah (Profit sharing saving or fixed time deposit account) and Murabaha (Cost-plus sale) respectively.

With regard to reason for not accessing IFB products and services offered by conventional banks, Table 4.6 shows that, 88 (40.36%) participants said, they were not interested since it is offered by conventional banks. In additions, 76 (34.86%) respondents' perceived IFB window services is not difference from conventional financial services.

### 4.2.7 Sources of Capital for Startup Business

This section addresses the result of questions presented for participants who were in business regarding to their source of finance to start up their business. The result summarized in the table below.

Table 4.7 Sources of Capital of Respondents in Business

| Question | Response | Frequency | Percent |
|---|---|---|---|
| Are you in Business? | yes | 98 | 100.0 |
| Did you take out a loan from any bank or any other financial institution when you were starting up your business? | Yes | 1 | 1.02 |
| | No | 97 | 98.98 |
| | Total | 98 | 100.0 |
| Did you approach any of the institutions offering interest free financial products for raising finance for your business? | Yes | 10 | 10.20 |
| | NO | 88 | 89.80 |
| | Total | 98 | 100.0 |
| What was your Source of fund when you start up business | Own Capital | 24 | 24.5 |
| | Family and friends | 52 | 53.06 |
| | Not answered | 22 | 22.44 |
| | Total | 98 | 100.0 |

As illustrate in Table 4.7, Out of the total 321 respondents, 98 (30.5%) were participated in Business. From those 98 who were in business, 97 respondents did not take loan from any financial institutions. In addition to this, 88 respondents did not ask any financial institution which offer interest free services.

As indicated in Figure 4.7, From 98 respondents who were in business, for 52 (53.06%) of the business owners, the source of finance for their business came from family and friends while 24(24.5%) participants start their business using their own capital.

### 4.2.8 Expectation from the Introduction of Full-Fledged Islamic Finance

This section provides the expectation of Ethiopian Muslims from the introduction of full-fledged Islamic finance.

Table 4.8 Plans of Muslims to Participate in Full-fledged Islamic Finance

| If full fledge Islamic finance in Ethiopia is started, how will you participate? | Frequency | Percent |
|---|---|---|
| I will be a customer | 207 | 64.5 |
| I will buy share | 108 | 33.6 |
| I will advertise it | 6 | 1.9 |
| I will not Participate | 0 | 0 |
| Total | 321 | 100.0 |

As can be seen in Table 4.8, if interest free finance introduced in Ethiopia, more than half of the participant (207, 64.5%) indicated they need to be a customer. Similarly, 108 (33.6%) of respondents indicated their interest to be a shareholder.

Participants were also asked to report what the contributions of full-fledge Islamic finance to Muslims in specific and for the country's economy in general. The result indicated that, participants perceived the introduction of full-fledge Islamic finance will bring the following main benefits:

- Increase the participation of Muslims in the financial system of the country.
- Balance the wealth distribution of the country.
- Enhances economic development.
- To reduction poverty

### 4.2.9 Attitudes towards Existing Financial Services and Islamic Finance

The attitudes of participants towards the existing conventional financial services and Islamic finance, was measured using 6 Likert scale questions. The result was analyzed using Principal Component Analysis (PCA).

#### 4.2.9.1 Factor Analysis

Factor analysis is a type of exploratory multivariate analysis that used to either to reduce the observing variables (factors) in a common factor (model) or to discover relations among factors (Yong & Pearce, 2013). So, factor analysis is important to understand the relationship between factors. As stated by Comrey & Lee (Cited in Yong & Pearce, 2013), to perform factor analysis, the recommended sample size is at least 300 respondents and the variables that are intended to analysis should have at least 5 to 10 observations. Our sample meets this criterion as the final sample size is 321 respondents.

In this research survey, there are six statements which were designed to measure the respondents' perception towards the existing financial services and Islamic finance in Ethiopia. The researcher wants to reduce these six statements in to a more manageable and meaningful category that enhance to get an underling perception and to make possible interpretation. Hence, PCA was utilized. Before running PCA, we test the sample size adequacy for factor analysis usually by Kaiser-Meyer- Olkin (KMO) and Bartlett`s test. The following table presents the result of these tests.

Table 4.9 KMO and Bartlett's Test Result

| | | |
|---|---|---|
| Kaiser-Meyer-Olkin Measure of Sampling Adequacy. | | .743 |
| | Approx. Chi-Square | 352.289 |
| Bartlett's Test of Sphericity | Df | 15 |
| | Sig. | .000 |

According to the above table, the KMO value is 0.74, which is above the commonly recommended value 0.6 (Field, 2009) and the Bartlett's Test of Sphericity was significant $\chi^2$ (15) = 353.289, p < .001. This KMO and Bartlett's Test of Sphericity result suggests the feasibility of running factor analysis for this study. Once the researcher decided to apply factor analysis, the next step is to choose the most appropriate method of data extraction. In this study, Principal component analysis (PCA) which is the most common method of data extraction was used.

As Smith (2002) stated, PCA is a technique of identifying patterns in data and expressing the data by their similarities and differences. After identifying the pattern of the data by reducing the number of dimensions, it is easy to compress the data. The following table is the result of factor analysis based on Principal Component Analysis and Varimax rotation with Kaiser Normalization.

Table 4.10 Total Variance Explained

| Component | Initial Eigenvalues | | | Extraction Sums of Squared Loadings | | | Rotation Sums of Squared Loadings | | |
|---|---|---|---|---|---|---|---|---|---|
| | Total | % of Variance | Cumulative % | Total | % of Variance | Cumulative % | Total | % of Variance | Cumulative % |
| 1 | 2.492 | 41.525 | 41.525 | 2.492 | 41.525 | 41.525 | 1.951 | 32.515 | 32.515 |
| 2 | 1.078 | 17.966 | 59.491 | 1.078 | 17.966 | 59.491 | 1.619 | 26.977 | 59.491 |
| 3 | .782 | 13.036 | 72.528 | | | | | | |
| 4 | .656 | 10.930 | 83.458 | | | | | | |
| 5 | .586 | 9.761 | 93.219 | | | | | | |
| 6 | .407 | 6.781 | 100.000 | | | | | | |

Extraction Method: Principal Component Analysis.

According to Pallant & Manual (2010), Kaiser’s criterion of retaining factors with eigenvalue greater than 1 was common method to decide how many factors to extract. Therefore, in this study, components with eigenvalue greater than 1 were retained. As it is shown in the table above, two factors (preference towards Islamic finance and inconvenience towards conventional financial services) with an Eigen value greater than one, (2.49 and 1.07) were found. The two-component solution explained a total of 59.49% of the variance, with component 1 contributing 41.52% and Component 2 contributing 17.96%. To support the interpretation of the two Components, varimax rotation was performed.

Table 4.11 Rotated Component Matrix for PCA Varimax Rotation

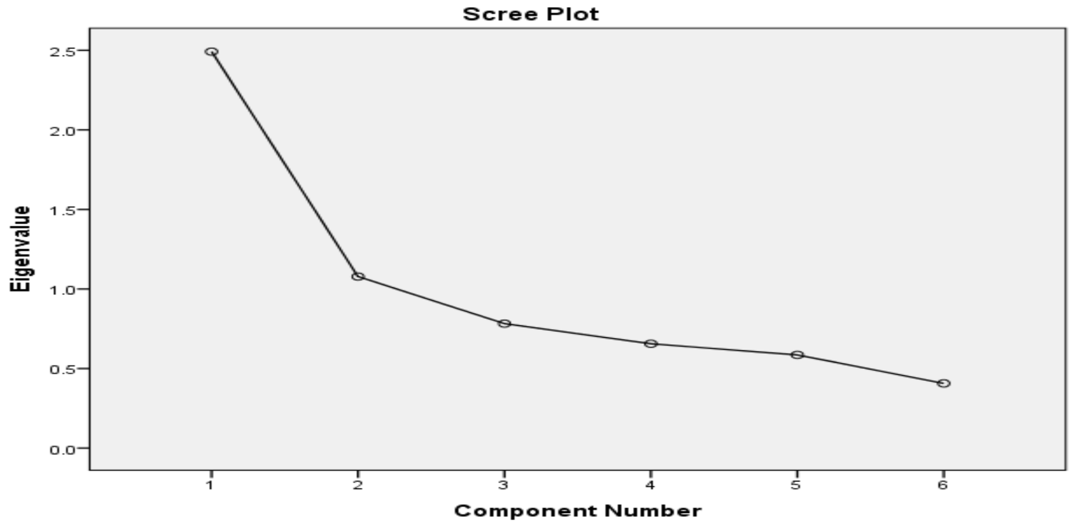
| Q. No. | Statements | Component 1 | Component 2 |
|---|---|---|---|
| 1 | The introduction of full-fledge Islamic finance in Ethiopia will enhance financial inclusion, poverty reduction and economic development. | **.800** | |
| 2 | By increasing access to full-fledged interest free financial products and services, the socio-economic status of Ethiopian Muslims will be improved (Example potential to acquire a property, participation in investment etc.) | **.765** | |
| 3 | If full-fledged Islamic finance introduce in Ethiopia, I prefer to access it. | **.684** | |
| 4 | The provision of interest free financial services by conventional banking window system is not encouraging Muslims to access it. | | **.820** |
| 5 | Historically, Ethiopian Muslims were known for trade and production, however in the current financial system, they are excluded from these sectors due to unavailability of sharia compliant financial sources. | | **.708** |
| 6 | There are many Ethiopian Muslims who are not accessing financial products and services due to religious reason and would do so if they had a real alternative. | .433 | **.598** |

Extraction Method: Principal Component Analysis.
Rotation Method: Varimax with Kaiser Normalization.
a. Rotation converged in 3 iterations.

According to the above rotated component matrix table, the six items have been reduced to two components. The next step is to look at the content of the six questions that load onto the same factor to try to identify common themes. Usually, researchers take a loading of an absolute value of more than 0.3 (Field, 2009). Therefore, by looking the pattern in rotated component matrix table, statement 1, 2 and 3 are load highly in component one while statement 4, 5 and 6 loads highly in component two. The questions in each component have the same characteristic and measure the same phenomenon. Questions in component one addresses the perception expressed by respondents about their **preference of full-fledged sharia compliant finance** by Ethiopian Muslims. On the other hand, questions in component two measures participants **inconvenience towards the existing conventional financial services**.

Furthermore, the scree Plot is a graph that shows Eigen values and component numbers. The below scree plot shows that the six variables are reduced to only two components as the graph slopes down steeply before becoming parallel to the x –axis. So, it is clear from the scree plot, there is a two-factor solution to this study.

Figure 4.1  Scree Plot




#### 4.2.9.2 Interpreting the Factor Analysis

The two-component solution to the attitude towards existing financial services and Islamic finance is summarized as follows:

**Component 1: The preference factors**

This component examines the preference expressed by Ethiopian Muslims regarding the full-fledged sharia compliant finance. As the below table illustrates, the level of agreement concerning the participant's preference of full-fledged sharia compliant finance was within the range of 95%-98%.

Table 4.12  Preference to Full-fledged Islamic finance

| No. | Statement | %of agreement* |
|---|---|---|
| 1 | The introduction of full-fledge Islamic finance in Ethiopia will enhance financial inclusion, poverty reduction and economic development. | 96.2% |
| 2 | By increasing access to Full-fledged IFB finance products and services, the socio-economic status of Ethiopian Muslims will be improved (Example potential to acquire a property, participation in investment etc.) | 97.5% |
| 3 | If full-fledged Islamic finance introduce in Ethiopia, I prefer to access it | 95.6% |

* By adding agree and strongly agree

**Component 2: Inconvenience factors**

The second component examines the inconvenience expressed by Ethiopian Muslims regarding the existing conventional financial services. The agreement level for these three statements was between 64.5%-79.1%. Hence, Inconvenience factors clearly shows that conventional financial services and IFB services on offer by conventional banks were not convenient for Ethiopian Muslims.

Table 4.13 Inconvenience Regarding to Services of Conventional Financial Institutions

| No. | Statement | %of agreement* |
|---|---|---|
| 4 | There are many Ethiopian Muslims who are not accessing financial products and services due to religious reason and would do so if they had a real alternative. | 73.5% |
| 5 | Historically, Ethiopian Muslims were known for trade and production, however, in the current financial system, they are excluded from these sectors due to unavailability of sharia compliant financial sources. | 79.1% |
| 6 | The provision of Islamic banking services by conventional banking window system is not encouraging Muslims to access financial products. | 64.5% |

*By adding agree and strongly agree

## 4.3 Quantitative (Interview) Analysis

In this section, the analysis of semi-structured interviews data collected from personnel of National Bank of Ethiopia and other commercial banks deliver IFB widow services is presented. These two groups were selected based on their direct relation with the issue of financial system. National bank of Ethiopia is on the authority of issuing financial regulations and other banks are rendering interest free banking services. The objective of this interview is to get in-depth information and enrich the data collected through quantitative tool.

Table 4.14 Details of Bankers Interviewed and Their Respective Institutions

| Name of Institution | Position of the Interviewee |
|---|---|
| National Bank of Ethiopia (NBE) | Bank Policy and Licensing Team |
| Oromia International Bank (OIB) | Vice-Manager, Interest free Banking |
| Commercial Bank of Ethiopia (CBE) | Manager, Interest free Banking |
| United Bank (UB) | Interest free financial Analyst |
| Nib International Bank(NIB) | Interest free financial Analyst |
| Wegagen Bank (WB) | Manager, Interest free Banking |
| Abay Bank(AB) | Manager, Interest free Banking |
| Cooperative Bank of Oromia(CBO) | Interest free financial Analyst |

### 4.3.1 Interview Questions for NBE

The following four basic questions were presented for personnel from national bank of Ethiopia.

#### 4.3.1.1 Analysis of Interviewee's Response Regarding to The Issuing of Directive NO. SSB/51/2011

The first interview question presented for interviewee from NBE was regarding the issuing of directive number SSB/51/2011. Explaining the reason why NBE issued the directive number SSB/51/2011, the interviewee stated that, the inquiry concerning the need of Interest free finance in Ethiopia was raised in 2008. In that time, Muslims were demanding a license for a full-fledged interest free finance by the name Zamzam Bank. Following their request, NBE was convinced on the importance of interest free finance to create an inclusive financial system. However, as the personnel stated, the most critical issue was on deciding about endorsing whether full-fledge or window system. After examining the experience of other countries like Malaysia, NBE decided to introduce interest free finance by window system.

#### 4.3.1.2 Does IFB Window fulfill Muslim's Need for Islamic Finance

Following this answer, the second interview question that was presented for the interviewee was concerning whether the above solution endorsed by NBE was adequate to satisfy the request of Muslim communities. Answering this question, the interviewee replied that the responsibility of NBE is to create opportunity for offering interest free finance. This was addressed by opening interest free window system. Therefore, the interviewee stated, there is no difference between offering interest free services through creating IFB window within the existing conventional banks and launching full-fledge interest free finance. Even though, the introduction of IFB window within conventional banks expected to enhance the participation of Muslims in the financial system, since the bank operates on the base of interest, it cannot give an opportunity for Muslims to be a shareholder or bank owner. This creates unequal wealth distribution among the population. Providing this, the researcher asked interviewee, if there is a way for Muslims to be a shareholder or bank owner which is free from interest. Addressing this question, the interviewee replied that this topic was not considered so far. According to the response given by the interviewee, the only concern of NBE was only in the context of service provision, not consider the other side importance of interest free finance for those who were not access conventional finance.

Giving the evidence from different literature which highlights the importance of introducing of full-fledged Islamic finance in Ethiopia in enhancing the financial inclusion of Ethiopian

Muslims, the interviewee was asked whether he agrees on such literatures or not. The interviewee indicated that he also agrees in the idea that introduction of full-fledge interest free finance would enhance the financial exclusion of Muslims.

The final interview question presented for personnel from NBE was concerning whether there is a plan to launch a full-fledged Islamic finance in Ethiopia. According to the interviewee, currently there is no any proposal in the NBE to permit full-fledged interest free finance in Ethiopia.

#### 4.3.2 Interview Questions for Commercial Banks

This section addresses the analysis of information collected from 7 conventional banks which provide interest free services by window system.

##### 4.3.2.1 Why Conventional Banks Launched IFB Window

The first interview question presented for personnel from Conventional Bank was about the reason why their respective institution offers interest free services by window system.

Table 4.15 Interviewee's Response for Interview question 1

| Q. 1 | What were the main reasons of your bank to introduce IFB services? |
|---|---|
| OIB | When the NBE issued the directive SSB/51/2011, We started IFB services to include the society who previously were not accessing finance because of religious reason. We know that there is a strong public need for these services. |
| CBE | The main reason to introduce these services was the issuing of SSB/51/2011 directive which helps to include in the financial system those who were not access conventional services. |
| UB | Introduction of this services enable us to find the huge customers who were not accessing conventional banks, and the growth of Islamic banking in the globe was also another pushing factor. |
| NIB | We can see the reason from two directions. When we see from local case our reason is customers need and SSB/51/2011 directive, and competition. When we see from International level, The expansion of IFB services and their profitability. |
| WB | The main reasons were the SSB/51/2011 directive, provide service for those excluded groups. |
| AB | The main reason is to provide services for those who were not accessing conventional services and their need for these services |
| CBO | Our reason was to include those who were not accessing finance due to religious reason, the expansion of Islamic finance in world and profit it has. |

As the above answer shows, the turning point to launch interest free services by conventional banks was the issuing of directive SSB/51/201. In addition to this, the reasons for the introduction of IFB window service in Ethiopia can be summarized in to the following main reasons: the strong demand from Muslim community, the expansion of IFB in the world, the profitability of opening the service by attracting the excluded Muslim community, and competition between banks.

#### 4.3.2.2 The Year IFB Started, Numbers of Branches with IFB Window and Numbers of IFB Accounts

The subsequent semi structured interview questions were regarding the time they start to offer IFB services, total number of branches and branches with IFB window and number of accounts in IFB window.

Table 4.16 Responses for Interview question 2, 3 & 4

| Question | Year IFB started | No. of Branches | Branches with IFB | No. of IFB accounts |
|---|---|---|---|---|
| OIB | 2013 | 216 | 204 | 132,587 |
| CBE | 2013 | 1167 | 777 | 446,133 |
| UB | 2014 | 160 | 160 | * |
| NIB | 2015 | 164 | 164 | 4078 |
| CBO | 2015 | 235 | 200 | * |
| WB | 2016 | 200 | 200 | 6000 |
| AB | 2016 | 140 | 43 | 3500 |
| **Total** | | **2,282** | **1,748** | **592,298** |

As stated in the above table, OIB and CBE are the first banks to launch interest free services through window system in 2013. Other banks launched IFB product between the year 2014 and 2016. From the total 2,282 branches of these seven banks, majority of them (1,784 branches) have IFB window. The customers of UB, NIB, WB and AB can access their IFB account in all branches of the bank. However, customers of OIB and CBE can access their IFB account only in branches which have IFB window. All over the country, the data from five banks indicated that, only 592,298 customers have IFB account in Conventional Banks.

#### 4.3.2.3 Products Offered in IFB Window

The fifth and sixth question of the semi structured interview questions were presented for the interviewee was about the kind of IFB services offered by their respective banks.

Table 4.17 Responses for Interview question 5&6

| Question | Products offering | Expected product |
|---|---|---|
| OIB | ○ Wadia, Amanah, Murabahah,<br>○ IF export financing | • Musharakah |
| CBE | ○ Wadia, Amana, Mudarabah<br>○ Financing (Murabahah) | • Ijarah, Salam, Istisna |
| UB | ○ Wadia, Amanah | • Qard, Musharakah |
| NIB | ○ Wadia, Amanah | • Murabahah, Istisna |
| CBO | ○ Wadia Current account and Saving account<br>○ Murabahah Financing | • Istisna, Ijarah, Kafalah |
| WB | ○ Wadia saving, Amanah | ▪ Qard |
| AB | ○ Wadia saving, Amanah | ▪ Murabahah |

In Ethiopia, IFB window services offered by Conventional banks divided in to three categories, namely deposit services (mainly *Wadia* Current account and *Amanah* Saving account), financing services (trade based like *Murabahah* and lease based like *ijara*) and other services (import and export financing). Of the seven banks, OIB, CBE and CBO provide both deposit and limited financing services while the rest four banks offer only deposit services.

#### 4.3.2.4 Switching of Customers from Conventional to IFB Window

Under question 7 of the semi structured interview I have tried to assess about the switching of customers from conventional to IFB window. However, before proceeding to presenting the result, it is important to describe the existing account types before the introduction of IFB window system.

Before the introduction of IFB window in Ethiopia, Conventional banks were providing a deposit service called Special Demand Account (SDA). From this account, Muslims were not collecting any interest or it is also known as zero interest account. Muslims were use this service only for safe keeping purpose in Convectional banks. When IFB window started, only WB converted this type of account in IFB window. Other banks continue to offer SDA in conventional banks. Hence, by this question, I have tried to examine whether the introduction of IFB window service make customers to switch their account (either conventional or SDA) to newly introduce IFB window accounts.

As the result in Table 4.18 below shows, there are some customers who switched from conventional to IFB window. Unfortunately, the interviewees could not provide a definite number.

Table 4.18 Switching of Customers from Conventional to IFB window

| Question | If your bank keeps records, how many Muslims have switched their conventional accounts to interest free banking account? |
|---|---|
| OIB | We did not record but there are customers switched to IFB |
| CBE | The number of our customers increase both in special account and IFB |
| UB | Some customers switched to IFB but we do not have the exact number |
| NIB | Some customer changed from conventional to IFB window |
| CBO | Some customers switched to IFB but we do not have the exact number |
| WB | We changed the account of our Muslim Customers to IFB |
| AB | Some customer changed from conventional to IFB window |

#### 4.3.2.5 Challenges While Offering IFB Window Services

The final question of the semi-structured interview was about the key challenges faced by the respective bank in the process of rendering IFB services. The interviewees reported the exitance of different challenges which are summarized in the bellow table.

Table 4.19 Challenges while Offering IFB Window Services

| Question | What are the key challenges your bank identified in rendering IFB services? |
|---|---|
| OIB | Skilled manpower shortage, problem regarding technology (core banking), legal issues, unavailability of framework by NBE, absence of independent Sharia Advisory and lack of public awareness. |
| CBE | Shortage of skilled and trained manpower in Islamic finance, and unavailability of ATM for IFB services. |
| UB | Problems related with legal issues, unavailability of proper reporting format to NBE and lack of public awareness. |
| NIB | The Skepticisms of customers, unavailability of Sharia advisory and shortage of skilled and trained manpower |
| CBO | Unavailability of Islamic bond (Sukuk), unavailability of detail directive from NBE and lack of scholars in Islamic finance. |
| WB | Absence of separate division in NBE which is responsible for IFB services, unavailability of Sharia advisory and Skilled manpower shortage. |
| AB | Lack of Public awareness and unavailability of Sharia advisory |

Among the main problems reported by interviewees while offering IFB window services were unavailability of framework by NBE, Shortage of skilled and trained manpower in Islamic finance, unavailability independent Sharia Advisory, lack of public awareness, the Skepticisms of customers and unavailability of proper reporting format to NBE.

# 5 DISCUSSION

This part of the paper discusses the results of the study in line with existing literatures. The overall objective of this study was to assess the extent and nature of religious driven financial exclusion of Muslims and the role of Islamic finance in tackling of religious driven financial exclusion in Ethiopia. As stated in the literature review, only few studies were conducted on religious driven financial exclusion and the role of Islamic finance in tackling of this exclusion.

Scholars such as Warsame (2009) and Mohieldin et al. (2012) suggested that Muslims who adhere to Islamic principles are not benefiting from conventional financial system or they are not accessing conventional financial services as it is against sharia principles. Similarly, the finding of this study indicates that 10.9% of the respondents did not use conventional saving services, 94.4% did not have access to credit, 69.2% did not have access to insurance, 87, 2% did not have access to micro finance, and 62.9% did not have access to home financing such as condominium housing program. This idea was also confirmed by the qualitative data collected through semi-structured interview. All interviewees stated that Ethiopian Muslims are not utilizing services rendered by conventional banks. Therefore, majority of Muslims refrains from accessing credit, insurance, microfinance and home financing.

Religion was the main factor for 45.7% participants not accessing bank saving, 65.3% for not accessing bank credit products, 57.7% for not accessing insurance, 58.6% for not accessing microfinance and 47.8% for not accessing home financing program. In addition to this, 73.5% of the respondents believe that many of Ethiopian Muslims are not accessing financial products and services due to religious reason. Similar finding was also reported by Ben et al. (2015) and World Bank (2014). These sources noted that Religious reason is one of the common causes for financial exclusion of Muslims across the world.

Ethiopian Muslims are excluded from conventional banks particularly state-owned banks (such as Commercial Bank of Ethiopia (CBE) and Development Bank of Ethiopia(DBE)), insurance services and microfinance institutions as well as from state-owned projects like condominium housing program. DBE was established to foster the countrywide development program through providing finance and close technical support to projects in priority area. Recently DBE is providing finance to long term investment projects in Agriculture, Argo-processing and Manufacturing. However, as the bank provides only interest based finances, Ethiopian Muslims did not get the opportunity to participate in the DBE's services.

As stated earlier, conventional financial systems in Ethiopia are against sharia principles. Although the majority of the respondents (89.1%) have access to savings, including special saving or salary account, 66.78% of them use their bank accounts with zero interest (interest free account) and 31.47% of them donate the interest income to poor people. This figure is exaggerated as compared to the country wide figure reported by World Bank 2014. According to World Bank (2014) report, only 14% of adults have saving account in conventional bank. The high number of participation reported in this paper regarding access to savings is mainly attributed to the fact that the data was collected from Addis Ababa, where substantial number of banks are concentrated. Through either using interest free banking or donating the interest to poor people, Muslim customers believe as they avoid interest which is prohibited by Islamic sharia. Saving money in Conventional banks either in interest free account or by collecting interest to donate it for poor peoples may result to losing the value of money (time value of money) comparing to other people who use the money with interest. Thukumar and Devamohan (2008) also reported evidence which strengthen this finding. They stated that Muslims avoid interest by opening interest free account or by donating the interest to the poor people. Muslims to improve their lives and contribute their part in the growth and development of their country, there should be financial institutions which comply with sharia principle and provide interest free credit.

Although, as a principle, sharia prohibits interest based financial transactions, some of the respondents use at least one of the conventional financial services. Their justification for the use of conventional financial services emanates from unavailability of alternative Sharia compliant financial services (48.5%) and mandatory nature of using some of the services like third party vehicle insurance coverage (29.5%). In Ethiopia, for example, it is obligatory for automobile owners to have third party vehicle insurance coverage. Due mainly to the contradiction of the provision of conventional financial services, Muslims are excluded and unable to prosper and contribute their part in the process of their community's or country's development. In line with this, 79.1% of the respondents suggested that Ethiopian Muslims cannot compete in trade activities and production due to unavailability of sharia compliant financial sources. It is also suggested that those Muslims who own their own business have got the capital to start up either from their family or friends. Bayrne and Anderson (2015) stated that there is no financial institution that offers Islamic finance for substantial number of the Muslim population who need sharia compliant finance. In the absence of sharia compliant financial services, it is by no means that Muslims compete with other groups of people in the country.

Ethiopian Muslims for many years were requesting the government for allowing them to open an Islamic finance, though the government did not permit them. They attempt to establish the first full-fledged Islamic bank with the name Zamzam Bank which was denied by NBE from having banking license in 2011. In the same year, NBE issued a new directive No. SSB/51/2011 that permitted conventional banks to offer interest free services through window system. One of the preambles of Directive No. SSB/51/2011 is the increasing of public demand for interest free banking in Ethiopia. Consequently, 8 conventional banks are now providing interest free services through window system. Even though the majority of the respondents (85%) knew interest free products are offered by conventional banks, 67.9% of them are not using these products. Despite the provision of Islamic banking services by conventional banking window system, Muslims are not encouraged to utilize this services due mainly to the interest-based services of conventional banks in Ethiopia. As inferred from semi-structured interviews, there is a mismatch between the public need for interest free finance and the NBE decision. Muslims' intention to open Islamic finance system or banking failed due to lack of interest from the government side as NBE permitted interest free services to be offered only by conventional banks. This decision dissatisfied many of Ethiopian Muslims who were eager to have banks that comply with sharia principles. The findings of this paper concur with Kerima's (2016). She noted that one of the challenges of interest free banking in Ethiopia is the service being offered by conventional banks.

Currently, throughout the world, Islamic banks are manifested in three forms such as full-fledged Islamic finance, Islamic /interest free Window and Islamic Subsidiaries Banks. However, the researcher has not find any literature that support or against the offering of interest free finance through window system. In the case of Ethiopia, interest free banking services offered by conventional banking failed to decrease religious driven financial exclusion as they are unable to create acceptability by Muslim communities who see sharia compliant financial services are not in place. The data collected through semi-structured interview shows that, all over the country, only 592,298 customers have IFB account in conventional banks. This clearly shows that the provision IFB services by conventional banks are not meeting its objective. The main objective of introducing IFB services in Ethiopia was to include in the financial system those who were not accessing conventional financial services due to religious reason. After four years of launching, out of more than 34 million Muslims, only half million of them have IFB accounts. So, we can conclude that, the introduced IFB service by conventional banks has failed to enhance the inclusion of Muslims in the financial system. This is may be because of the refusing of NBE to give full-fledged Islamic banking license to Muslims. The decision of NBE not to allow Muslims to open Islamic banking is against the constitutional provision that allow citizens to engage in economic activities. For example, article 41; sub-Article 1 of the constitution gives the right to engage freely in economic activity. However, the new directive promulgated in 2011, Directive No. SSB/51/2011 closed the door for potential Muslims to participate in banking business. So, there is a discrepancy between the demand of Muslims and the decision of NBE.

Currently, IFB window services offered by conventional banks are very limited and targeted only deposit collection from Muslim communities. The vice governor of NBE examined the current level of IFB deposit mobilization and said that the deposit collected through IFB window are very insignificant and it is less than 1 percent of the deposit mobilized by commercial banks. Though he did not yet recognize the need of Ethiopian Muslims in establishing a full-fledged sharia compliant financial institution that can boom Muslims' engagement in different production and investment activities.

As indicated in the result section, if full-fledged interest free finance is allowed in Ethiopia, all participants have interest to participate either by buying of shares or by being customer or by advertising it. In support of this, the two-component result of factor analysis shows that, Ethiopian Muslims prefer the full-fledged sharia compliant finance and inconvenience with the existing conventional financial services. Such strong demand among Muslims for the introduction of Islamic banking system in Ethiopia is consistent with the findings of Thukumar and Devamohan (2008) who noted Ethiopian Muslims need separate Islamic bank (Full-fledged) as most of them are interested to open account and to take initiative if Islamic banking is allowed in Ethiopia.

Considering the role of full-fledged interest free finance in Ethiopia, 97.5% respondents believe that, if full-fledged Islamic finance is allowed in Ethiopia, it will play a significant role in tackling of financial exclusion, poverty reduction, enhancing economic development and equitable distribution of income. In support of this, Scholars such as Mohieldin et al (2012), and Naceur et al (2015), argued that Islamic finance have a potential to enhancing financial inclusion by offering sharia compliant financial services. Akhter, Akhtar and Jaffri (2009) and Dhaoui (2015) assert that Islamic financial institutions especially Islamic microfinance institutions play vital roles in order to alleviate poverty in developing countries. Likewise, Sarwer et al. (2013) and Rabaa and Younes (2016) noted that Islamic finance have a potential to enhance economic development and Islamic finance positively and significantly relevant with economic growth.

# 6 CONCLUSION AND RECOMMENDATION

## 6.1 Introduction

The main objective of this study was to assess the extent and nature of religious driven financial exclusion of Muslims in Ethiopia and the role of Islamic finance in tackling of religious driven financial exclusion. Based on the collected data through questionnaire and sub-structured interview and analysis, this part provided the conclusions drawn from analysis and provides possible recommendations to different stakeholders.

## 6.2 Conclusion

The foregoing analysis result and discussion has led to the following conclusions.

First, the conventional financial institutions of Ethiopia such as banks, insurance companies, microfinance institutions and home financing (condominium housing program) did not accommodate the special interests of Ethiopian Muslims for interest free financial service. As it is described in the result section, from total participants, 94.4% had not accessed credit, 69.2% had not accessed insurance, 87,2% had not accessed micro finance and 62.9% had not accessed home financing.

Second, majority of Ethiopian Muslim refrain from accessing conventional financial services because of religious reason. Therefore, the financial exclusion of Ethiopian Muslims is religious driven.

Third, the new introduced interest free window was not adequate to enhance the inclusion of Muslims in the financial system. Despite the participants know about interest free window, most of them were not using it. This is mainly resulted from the skepticism of Muslims about interest free window. This implies the presence of discrepancy between the need of Ethiopian Muslims for full-fledged Islamic finance and the response of NBE by interest free window/Islamic window.

Fourth, the absence of full-fledge Interest free financial institution in Ethiopia affected the participation of Muslims in economic activity. The financing source of Muslims in business are limited with own capital and borrowing from family and friend. Therefore, they cannot participate in an investment that needs huge capital.

Fifth, almost all participants need the establishment of Full-fledged Islamic finance. If NBE allows the establishment of such institution, Muslim communities will participate by being customer, by buying share, or by advertising it.

Finally, the introduction of full-fledged Islamic finance will enhance financial inclusion of Muslims which will help to alleviate poverty and enhance economic development.

### 6.3 Recommendation

In this section, I propose recommendations that could be considered for enhancing the inclusion of Ethiopian Muslims in the financial system for stakeholders such as Government, National Bank of Ethiopia (NBE), Development Bank of Ethiopia (DBE), Interest Free banking (IFB) window providers, Ethiopian Islamic Affairs Supreme Council (EIASC), Muslim communities and educational institutions.

- ☞ The financial access and inclusion in Ethiopia is at lower level due to different causes. Ethiopian Muslims in particular are not benefiting from the existing conventional financial system of the country due to religious reason. Therefore, it is important if the government of Ethiopia considers religious issues when developing financial policies and regulations like Condominium program. A good example for such experience can be England by the introduction of Islamic home financing for population which is less than one tenth of Ethiopian Muslims.
- ☞ The need of Ethiopian Muslims for Sharia compliant financial services is clear and net. They need both the interest free service and participating in the ownership of financial institutions. But, the regulatory framework does not allow that. There is no regulatory framework that permits the establishment of interest free insurance and microfinance. Even the directive issued regarding to interest free banking also does not permit the establishment of full-fledged interest free banking. Therefore, NBE should develop regulatory and supervision framework that support wide financial inclusion. Among

the practical measures that have to be taken by NBE is allowing the establishment of full-fledged interest free financial institutions such as interest free banking, insurance and microfinance institutions.

The establishment of these institutions is important to:

- ✓ Tackling financial exclusion

Islamic financial institutions have a potential to minimize financial exclusion by providing sharia compliant financial services for those who are not accessing conventional financial services due to religious reason. In doing so, the financial system of Ethiopia will be an inclusive financial system.

- ✓ Alleviate poverty

Employing interest free financial services for those who are not accessing conventional finances will be a valuable tool to alleviate poverty.

- ✓ Encourage entrepreneurship

Most of commercial banks in Ethiopia did not provide finance for entrepreneurs who have only a project idea. In contrast, Islamic finance support entrepreneurs by profit and loss sharing mode of financing. Employing this mode of financing offers important profit opportunity to Islamic financial institutions and encourage entrepreneurship and economic growth.

- ☞ One of the communal problem identified by IFB window providers is the absence of division within NBE that control the activities of IFB window. Hence, NBE should create a division that is responsible for the issue of interest free finance within the structure of NBE and should assign sharia advisory to check whether the IFB window services are operating in accordance with sharia principles.
- ☞ DBE is established to support the development of the country by providing finance to viable projects. But, all financial products of DBE are only interest based which is against sharia principles. Due to this Muslims are not benefiting from this financial opportunity as a nation. Therefore, DBE should think alternative sharia compliant financial products to Muslims who are not using interest based financial products.

- EIASC is a responsible institution to enforce the rights and benefits of Muslims. Therefore, it is expected from EIASC to work with the government to look a way for the establishment of Islamic financial institution. In addition to this, EIASC should take an initiative to institutionalize Islamic wealth redistribution instruments viz. *Zakat, Waqf, Sadaqa* and *qard al-Hassan*. Institutionalization of these instruments is important to enhance the financial inclusion of Muslims.
- This study shows that there is a skepticism about IFB window services in Ethiopia. Therefore, interest free window providers should check their services in accordance with sharia principle, make clear their products and working procedures, provide products further than deposit collection, modifying marketing strategy and develop products suitable for Muslims.
- The ownership of IFB windows are still on the hands of conventional banks. To allow the participate Muslims in the ownership of banks, IFB window providers should segregate the capital of IFB window or establish IFB through subsidiaries to offer separate share of IFB for public. These can create a room for Muslims to participate in the ownership IFB.
- Ethiopian Muslims have been requesting the government for many years to permit interest free finance. However, NBE permitted only interest free window. Therefore, Muslim Communities should continue demanding for the licensing of full-fledged interest free banking, insurance and Microfinance institutions. In addition to this, to empower the economically weak Muslim societies, Ethiopian Muslims have to work with EIASC to formalize Islamic wealth redistributive instruments viz. *Zakat, Waqf, Sadaqa* and *qard al-Hassan.* Muslim scholars, Religious leaders, Islamic associations and Islamic Medias also should create awareness about Islamic financial institutions, its products and services and its importance for Muslim communities and for economic development of the country.
- In Ethiopia, there is a shortage of professionals in Islamic finance. There is no any educational institution that give training and education about Islamic finance. Globally the demand is increasing for Education in Islamic finance. Therefore, Educational Institutions in Ethiopia should give Islamic finance courses to solve the shortage of talented professionals in Islamic finance.

## 6.4 Limitation of the Study

Due to time and financial shortages, the study was conducted only in Addis Ababa. These limits the finding of this study from making adequate generalization. Lack of enough literature regarding the topic in Ethiopia was also one of the limitations.

## 6.5 Further Research Suggestions

The followings are some of the areas where further study could be conducted:

1. The potentiality of Islamic Microfinance in Ethiopia
2. The potentiality of Islamic insurance(Takaful)
3. Institutionalization of Islamic wealth redistribution instruments viz. *Zakat, Waqf, Sadaqa* and *qard al-Hassan* in Ethiopia
4. The consequences of Financial exclusions of Muslims in Ethiopia
5. Further studies can also be conducted on the same topic of this study by covering all regions of Ethiopia.

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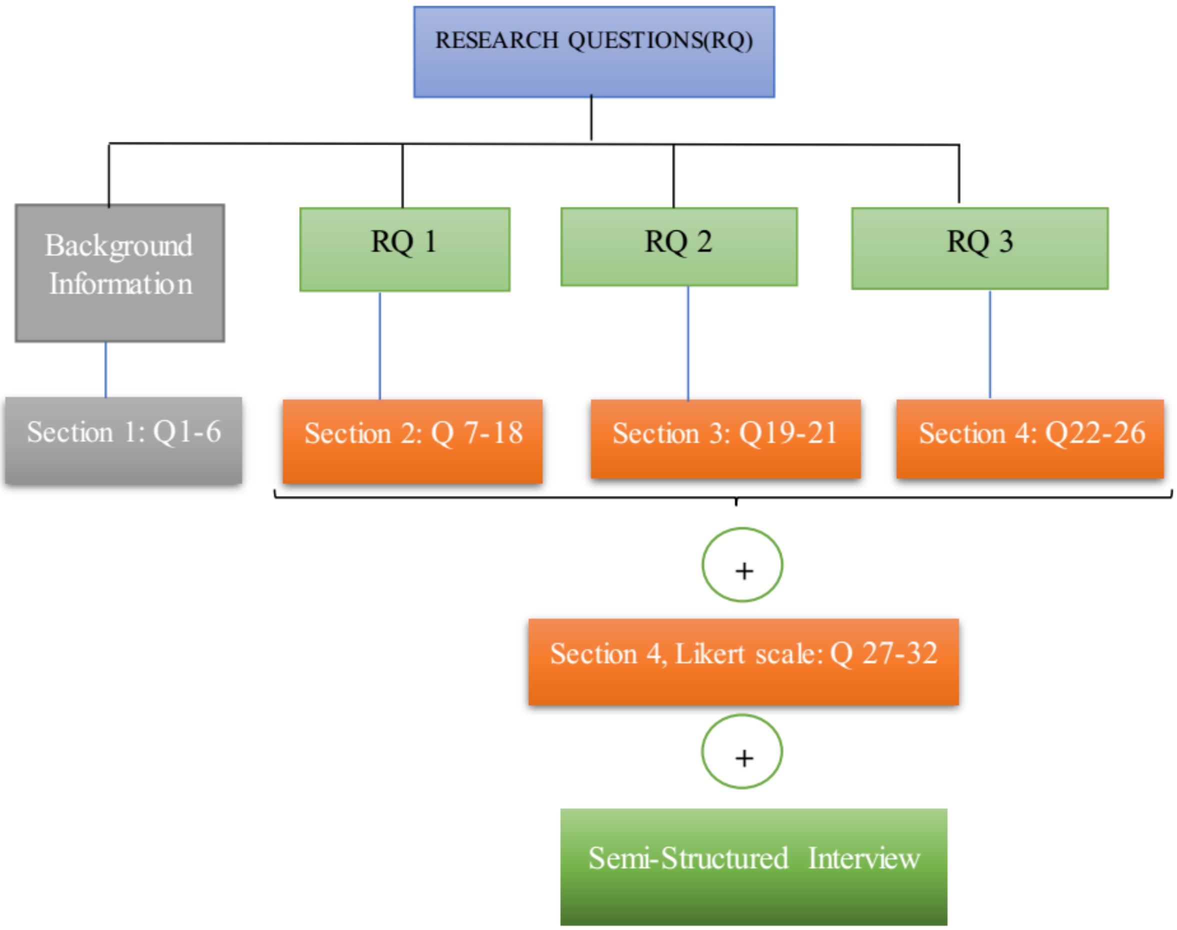
APPENDICES

## Appendix A: Likert Scale Questions Result Summery

| No. | Statements | Strongly disagree | Disagree | Neutral | Agree | Strongly agree | % of Agreement |
|---|---|---|---|---|---|---|---|
| 27 | There are many Ethiopian Muslims who are not accessing financial products and services due to religious reason and would do so if they had a real alternative. | 23 (7.2%) | 39 (12.1) | 23 (7.2%) | 89 (27.7%) | 147 (45.8%) | **73.5%** |
| 28 | The introduction of full-fledge Islamic finance in Ethiopia will enhance financial inclusion, poverty reduction and economic development. | 3 (0.9%) | 4 (1.2%) | 5 (1.6%) | 87 (27.1%) | 287 (69.1%) | **96.2%** |
| 29 | By increasing access to Islamic finance products and services, the socio-economic status of Ethiopian Muslims will be improved (Example potential to acquire a property, participation in investment etc.) | 3 (0.9%) | 1 (0.3%) | 4 (1.2%) | 99 (30.8%) | 214 (66.7%) | **97.5%** |
| 30 | Historically, Ethiopian Muslims were known for trade and production., however, in the current financial system, they are excluded from these sectors due to unavailability of sharia compliant financial sources. | 9 (2.8%) | 30 (9.3%) | 27 (8.4%) | 123 (38.3%) | 131 (40.8%) | **79.1%** |
| 31 | The provision of Islamic banking services by conventional banking window system is not encouraging Muslims to access financial products. | 9 (2.8%) | 37 (11.5%) | 68 (21.2%) | 115 (35.8%) | 92 (28.7%) | **64.5%** |
| 32 | If full-fledged Islamic finance introduce in Ethiopia, I prefer to access it | 9 (2.8%) | 1 (0.3%) | 4 (1.2%) | 27 (8.4%) | 280 (87.2%) | **95.6%** |

% of Agreement: Agree and Strongly agree

**Appendix B: The relationship between research questions and Data collection tools**



## Appendix C: Permission to use existing survey Tool

Permission to use existing survey

**suadiq mohammed** <suadiq1434@gmail.com> Tue, Jan 17, 2017 at 3:26 PM

To: mhwarsame5@hotmail.com

Dr. Mohammed Hersi Warsame,

I am a student from Ankara Yildirim Beyazit University writing my thesis titled "The role of Islamic finance in combating financial exclusion in Ethiopia" under my advisor Assoc. Prof. Dr. Ayhan Kapusuzoğlu.

I would like your permission to use "The role of Islamic finance in tackling financial exclusion in the UK" questionnaire instrument partially and as a reference to prepare in my research questionnaire. I would like to use your survey under the following conditions:

- I will use some part of surveys and as reference to prepare my questionnaires only for my research study and will not sell or use it with any compensated or curriculum development activities.
- I will send a copy of my completed research study to your attention upon completion of the study.

Sincerely.
Suadiq Hailu

---

**Mohammed Warsame** <mhwarsame5@hotmail.com> Tue, Jan 17, 2017 at 4:28 PM
To: suadiq mohammed <suadiq1434@gmail.com>

Ok. That is fine. You can go ahead but keep me posted.

Mohammed

Dr. Mohammed Warsame (BSc, MSc, Ph.D, FCCA, CIPA)
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College of Business Administration
University of Sharjah
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United Arab Emirates
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## Appendix D: Questionnaire (English version)

The Role of Islamic Finance in Combating of Financial Exclusion in Ethiopia
For MSc of Banking and Finance

Dear Sir/Madam,

I am a student at the institute of social science, Banking and Finance MSc degree program in Ankara Yildirim Beyazit University, Turkey. I would like to invite you to participate in this survey regarding to the followings:

- ❖ The purpose the study is to assess the nature and extent of financial exclusion of Muslims in Ethiopia and to find out the introduction of full-fledged Islamic finance in Ethiopia can significantly enhance the level of financial access to Ethiopian Muslims.
- ❖ Financial exclusion exist when individuals or communites do not have access to fair, safe and affordable financial products and services.

Please answer the following question based on instructions in each part as correctly as you can. The correctness of your answer will determine the quality of the research outcome. Be confidential that your personal response will not expose in public area.
Alongside this letter is the questionnaire which will take about 10 minutes to finish. I would like to say Thank you in advance for your time, commitment and participation in this survey.

Best regards,
Suadiq Mehammed Hailu
Mobile: +90 505 367 0662
Email: Suadiq1434@gmail.com

### Section 1: personal information

1. Your Age:
   - ☐ 18 – 30 ☐ 31 – 40
   - ☐ 41 – 50 ☐ 51 – 60 ☐ Above 60 years
2. Your Gender:
   - ☐ Male ☐ Female
3. Marital Status:
   - ☐ Married ☐ Single ☐ Divorced
4. Your Education Level
   - ☐ No Education ☐ Primary School
   - ☐ Secondary School ☐ High School
   - ☐ Vocational Training School ☐ Degree ☐ Master
   - ☐ PhD
   - ☐ Others, please specify.....................
5. Your Current Occupation:
   - ☐ businessman/businesswoman ☐ Employed
   - ☐ Student ☐ Unemployed

- ☐ Retired
- ☐ Others, please specify………

6. Your Monthly Income (In Ethiopian Birr):
   - ☐ Less than 1,500
   - ☐ 1,501 – 3,000
   - ☐ 3.001 – 4,500
   - ☐ 4,501 – 6,500
   - ☐ 6,501 – 7,500
   - ☐ 7,501 – 10,000
   - ☐ More than 10,000

**Section 2: your access to conventional financial products and services in Ethiopia**

7. Do you have any of the following accounts with a conventional bank?
   - ☐ Saving Account
   - ☐ Current (Checking) Account
   - ☐ Time Deposit
   - ☐ Special Saving Account
   - ☐ Salary Account
   - ☐ None
   - ☐ Others, please specify ______________________________________
8. If your answer for question 7 is "None" what was the reason?
   - ☐ I don't want to deal with interest
   - ☐ I don't need to save
   - ☐ I don't have enough money to save
   - ☐ I have tried but not successful
   - ☐ Others, please specify ______________________________________
9. If you save your money in conventional bank, for what purpose do you use the interest from your saving?
   - ☐ I save in special account/without interest
   - ☐ I give the interest to the poor people
   - ☐ I use the interest with principals
10. Do you access any of the following financial products with a conventional bank?
    - ☐ Home (Mortgage) Loan
    - ☐ Automobile Loan
    - ☐ Personal Loan
    - ☐ Business Loan
    - ☐ Educational Loan
    - ☐ None
    - ☐ Others, please specify ______________________________________
11. If your answer for question 10 is "None" what was the reason?
    - ☐ I don't want to deal with interest
    - ☐ I don't need to borrow
    - ☐ I don't know how to apply
    - ☐ I have tried but not successful
    - ☐ Others, please specify ______________________________________
12. Do you have a conventional insurance such as?
    - ☐ Home Insurance
    - ☐ Third party car Insurance
    - ☐ Personal Insurance
    - ☐ Medical Insurance
    - ☐ Others, please specify ______________________________________
    - ☐ None
13. If your answer for question 13 is "None" what was the reason?
    - ☐ Insurance products are against religious principles
    - ☐ I have tried but not successful
    - ☐ Others, please specify ______________________________________
14. Do you have any of the following financial products and services with a conventional Microfinance institutions?
    - ☐ Loan services
    - ☐ Saving services
    - ☐ Others, please specify ______________________________________
    - ☐ None

15. If your answer for question 15 is "None" what was the reason?
    - ☐ I don't want to deal with interest ☐ I don't need to borrow/save
    - ☐ I have tried but not successful
    - ☐ Others, please specify
16. Did you register for a condominium house program?
    - ☐ No ☐ Yes
17. If you say "No" to question 17, what was the main reason to not participate in condominium house?
    - ☐ I don't want to deal with interest ☐ I have tried but not successful
    - ☐ Others, please specify ______________________________________
18. If you are accessing conventional banking, insurance and micro finance products and condominium house program, as a Muslim what is your justification to use these products and services?
    - ☐ unavailability of alternative Sharia compliant products and services
    - ☐ you do not believe they are not noncompliant with Sharia
    - ☐ accessing is mandatory
    - ☐ Others, please specify ______________________________________

**Section 3: your access and knowledge about interest free banking services**

19. Do you know interest free financial services are being offered in Ethiopia by conventional banks?

☐ No ☐ Yes

20. Do you have access to any of the following interest free banking services offered by conventional banks?
    - ☐ Wadiah (Saving account) ☐ Amanah (Current account)
    - ☐ Mudharabah (Profit sharing saving or fixed time deposit account)
    - ☐ Murabaha (Cost-plus sale) ☐ None
    - ☐ Others, please specify ______________________________________
21. If you say none to question 19, what was the main reason for not accessing interest free banking services with conventional banks?
    - ☐ I am not interested as they are being offered by conventional banks
    - ☐ I am not interested as they are not different from conventional finances
    - ☐ I have applied but was not successful
    - ☐ Others, please specify ______________________________________

**Section 4: your expectation from the introduction of full-fledged Islamic finance**

22. If full fledge Islamic finance in Ethiopia will be started, how can you will participate?
    - ☐ I will be a customer
    - ☐ I will buy a share
    - ☐ I will advertise it
    - ☐ I will not want to participate
23. Are you in business?
    - ☐ No

- ☐ yes, please explain the type of business and the method of financing it ____

______________________________________________________________________

______________________________________________________________________

______________________________________________________________________

______________________________________________________________________

24. Did you take out a loan from any bank or any other institution when you were starting up the business?
    - ☐ No
    - ☐ yes, please explain the nature of the loan and from which institution _____

______________________________________________________________________

______________________________________________________________________

______________________________________________________________________

______________________________________________________________________

25. Did you approach any of the institutions offering interest free financial products for raising finance for your business?
    - ☐ No
    - ☐ yes, please explain what the outcome ________________________________

______________________________________________________________________

______________________________________________________________________

______________________________________________________________________

26. If full-fledge sharia complaint finance introduced in Ethiopian, what will be the contributions to Muslims in specific and for the country's economy in general?

______________________________________________________________________

______________________________________________________________________

**Section 5: your attitudes towards financial exclusions and interest free banking services offered in Ethiopia**

| Scale | | Please tick (✓) in the appropriate box | | | | |
|---|---|---|---|---|---|---|
| | | 1 | 2 | 3 | 4 | 5 |
| | | Strongly Disagree | Disagree | Neutral | Agree | Strongly Agree |
| 27 | There are many Ethiopian Muslims who are not accessing financial products and services due to religious reason and would do so if they had a real alternative. | | | | | |
| 28 | The introduction of full-fledge Islamic finance in Ethiopia will enhance financial inclusion, poverty reduction and economic development | | | | | |
| 29 | By increasing access to Islamic finance products and services, the socio-economic status of Ethiopian Muslims will be improved (Example potential to acquire a property, participation in investment etc.) | | | | | |
| 30 | Historically, Ethiopian Muslims were known for trade and production., however, in the current financial system, they are excluded from these sectors due to unavailability of sharia compliant financial sources. | | | | | |
| 31 | The provision of interest free financial services by conventional banking window system is not encouraging Muslims to access it. | | | | | |
| 32 | If full-fledged Islamic finance introduce in Ethiopia, I prefer to access it | | | | | |

## Appendix E: Semi-structured Interview Questions

### Interview Questions for the National bank of Ethiopia

1. Why NBE issued the directive number SSB/51/2011?
2. The new issued regulation permitted only interest free window i.e. only convectional banks offer interest free services. Do you believe that this window system can satisfy the strong public demand for interest free services?
3. According to different literature, there was a reasonable expectation that the introduction of full-fledged Islamic finance in Ethiopia would greatly enhance the financial inclusion of Ethiopian Muslims, do you think this was a reasonable expectation?
4. Does NBE have a plan to launch a full-fledged Islamic finance in Ethiopia?

## Interview Questions for the Interest Free Banking Directors

1. What was the main reasons of your bank to introduce IFB services?
2. How long have your bank been providing these services?
3. How many branches of your bank are providing interest free banking products and services?
4. How many people does open IFB account in your bank?
5. What are the interest free banking products and services your bank offer?
6. Which are the products and services your bank planned to offer in the future?
7. If your bank keeps records, how many Muslims have switched their conventional accounts to your interest free banking account?
8. In Ethiopia, there is no authorized body who checks the interest free banking products and services weather they are compliant with sharia principle or not. What is your response to this idea?
9. What are the key challenges your bank identified in rendering IFB services?

## Appendix F: Questionnaire (Amharic Version)

**የመጠይቅ ቅፅ**

እኔተማሪሳዲቅመሐመድበቱርክአንካራይልድሪምበያዚት /Yildirim Beyazit / ዩኒቨርሲቲሁለተኛዲግሪዬንበባንኪንግእናፋይናንስእየተማርኩእገኛለሁ።የመመረቂያፅሑፌን *"ከወለድነፃየፋይናንስአገልግሎቶች ፋይናንስን ለሁሉም ማህበረሰብ ተደራሽ ለማድረግ የሚያበረክቱት አስተዋጽኦ"* በሚል ርዕስ ላይ እየሰራሁ እገኛለሁ።

ለዚሁጥናትግብዓትብቻየተዘጋጀዉንይህንንየመጠይቅቅፅለመሙላትተሳታፊእነዲሆኑስጋብዝዎትከትልቅምስጋናጋርነዉ።

- ❖ የዚህጥናትዓላማበሀይማኖትምክንያትከመደበኛፋይናንስአገልግሎቶችእራሳቸዉንያገለሉየማህበረሰብክፍሎችምንያህልእነደሆኑ፣ ሙስሊሞችበመደበኛባንኮችስለሚሰጡትከወለድነፃየባንክአገልግሎትያላቸዉአመለካከት፣ ሙሉየሆነከወለድ ነፃፋይናንስቢጀመርፋይናንስንለሁሉምማህበረሰብተደራሽለማድረግየሚያበረክተውአስተዋጽኦእናሙስሊሙማህበረሰብስለወለድ ነፃፋይናንስያለዉንየእዉቀትደረጃለመለካትነው።

- ○ ይህንመጠይቅበትክክልመሙላትዎየጥናቱንዉጤትትክክለኛነትይወስነዋል።
- ○ ለዚህመጠይቅየሚሰጡትመልስሚስጥራዊእናለሌላአካልተላልፎአይሰጥም።
- ○ ይህንመጠይቅለመሙላትበግምት 10 ደቂቃሊወስድብዎትይችላል።
- ○ እባክዎ በትክክለኛ ምርጫዎ ላይ የ (✓) ምልክት ያድርጉ።
- ○ ጥያቄውን መሰረት በማድረግ ከአንድ በላይ ምርጫዎች ላይ ምልክት ማድረግ ይችላሉ።
- ○ ጊዜዎንመስዕዋትአደርገዉቅፁንለመሙላትስለተባበሩንከወዲሁአመሰግናለሁ።

ከሰላምታጋር
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Mobile: +251944211035
Email: Suadiq1434@gmail.com

### I. የግልመረጃ

1. ዕድሜ፡

☐ 18 – 30 ☐ 31 – 40 ☐ከ 61 በላይ

☐ 41 – 50 ☐ 51 – 60

2. ፆታ፡

☐ወንድ☐ሴት

3. የጋብቻሁኔታ፡

☐ያገባ☐ያላገባ☐የፈታ

4. የትምህርትደረጃ፡

☐መደበኛትምህርትያልጀመረ☐አንደኛደረጃትምህርት

☐ሁለተኛደረጃትምህርት☐ሞያናቴክኒክ

☐የመጀመሪያዲግሪ☐ሁለተኛዲግሪ

☐ 3ተኛዲግሪ (ፒኤችዲ) ☐ሌላከሆነይግለጹ..................................

5. የስራሁኔታ፡

☐ነጋዴ☐ተቀጣሪ

☐ተማሪ☐ስራፈላጊ

☐ጡረተኛ ☐ ሌላ ከሆነ ይግለጹ .............................................

6. ወርሃዊገቢ (በብር):

☐ከ 1,500 በታች☐ 1,501 – 3,000

☐ 3,001 – 4,500 ☐ 4,501 – 6,500

☐ 6,501 – 7,500 ☐ 7,501 – 10,000

☐ከ 10,000 በላይ

## II. <u>የመደበኛባንክአገልግሎትተጠቃሚነት</u>

7. እርስዎከሚከተሉትየመደበኛባንክሂሳብ የትኛውን/የትኞቹን ይጠቀማሉ?

☐የቁጠባሂሳብ☐ከረንት አካውንት(ቼክ)

☐ታይምዲፖዚት☐ልዩየቁጠባሂሳብ

☐የደመዎዝመክፈያሂሳብ ☐ ሂሳብ የለኝም

☐ሌላከሆነይግለጹ ________________________________________

8. ለጥያቄቁጥር 7 መልስዎሂሳብየለኝምከሆነምክንያትዎምንይሆን?

☐ባንኮችወለድንመሰረትያደረጉስለሆነናወለድ ከሀይማኖቴጋርስለሚጻረር

☐መቆጠብስለማልፈልግ

☐የምቆጥበዉገንዘብስለሌለኝ

☐ሂሳብ ለመክፈት ሞክሬ ስላልተሳካልኝ

☐ሌላከሆነይግለጹ ________________________________________

9. ገንዘብዎትንከመደበኛባንኮችዘንድየሚያስቀምጡከሆነወለዱንለምን አገልግሎት ያውሉታል?

☐ወለድበማይታሰብበትሂሳብነዉየምቆጥበዉ ☐ወለዱንተቀብዬለድሆችእሰጠዋለሁ

☐ወለዱንከመነሻገንዘቤጋርእጠቀመዋለሁ

10. ከመደበኛ ባንክከሚከተሉትየብድርአይነቶችየትኛውን/የትኞቹን ተጠቅመዉያውቃሉ?

☐ለቤትመስሪያ☐ለአዉቶሞቢል

☐ለግልወጪ☐ለስራ

☐ለትምህርት☐ተበድሬ አላውቅም

☐ሌላከሆነይግለጹ ________________________________________

11. ለጥያቄቁጥር 8 መልስዎተበድሬ አላውቅምከሆነምክንያትዎምንይሆን?

☐ባንኮችወለድንመሰረትያደረጉስለሆነናወለድ ከሀይማኖቴጋስለሚጻረር

☐መበደርስለማልፈልግ ☐ለመበደር ሞክሬስላልተሳካልኝ

☐ሌላከሆነይግለጹ ________________________________________

12. ከሚከተሉትየኢንሹራንስፕሮግራሞችመካከልየትኛዉንይጠቀማሉ?

☐የቤትኢንሹራንስ☐የተሽከርካሪኢንሹራንስ

☐የህይዎትኢንሹራንስ☐የጤናኢንሹራንስ

☐ የሶስተኛ ወገን የተሽከርካሪ ኢንሹራንስ☐የለም

☐ሌላከሆነይግለጹ ________________________________________

13. ጥያቄቁጥር 13 ላይየተጠቀሱትንየኢንሹራንስአገልግሎቶችንተጠቃሚካልለሆኑምክንነያተዎምንይሆን?

☐አገልግሎቶቹ ከሀሄይማኖቴጋስለሚጻረሩ☐ሞክሬስላልተሳካልኝ

☐ሌላከሆነይግለጹ ________________________________________

14. ከሚከተሉትየጥቃቅንናአነስተኛየገንዘብተቋማትአገልግሎቶችየትኛዉንይጠቅማሉ?

☐የብድርአገልግሎት☐የቁጠባአገልገሎት

☐ሌላከሆነይግለጹ ____________________________________________ ☐የለም

15. ጥያቄቁጥር

15ላይየተጠቀሱትንየጥቃቅንናአነስተኛየገንዘብተቋማትአገልግሎቶችንተጠቃሚካልለሆኑምክንነያተዎምንይሆን?

☐ወለድንመሰረትያደረገስለሆነናወለድ ከሀሄይማኖቴጋስለሚጻረር

☐መቆጠብወይምመበደርስለማልፈልግ ☐ሞክሬስላልተሳካልኝ

☐ሌላከሆነይግለጹ ____________________________________________

16. የጋራመኖሪያቤትቶች (condominium house) ተመዝግበዋል?

☐አዎ☐አልተመዘገብኩም

17. ለጥያቄቁጥር 18መልስዎ "አልተመዘገብኩም" ከሆነምክንነያተዎምንነበር?

☐ከፍያዉወለድንመሰረትያደረገስለሆነናወለድ ከሀይማኖቴጋስለሚጻረር

☐ሞክሬስላልተሳካልኝ ☐ሌላከሆነይግለጹ...............................................

18. እርስዎሙስሊምከመሆንዎአንጻርከባንክ፣ከኢንሹራንስ፣

ከጥቃቅንአናአነስተኛተቋማትወይምየጋራመኖሪያቤትቶችፕሮግራምየአንዱንአገልግሎትተጠቃሚከሆኑለመጠቀምያነሳ

ሳዎትምክንያትምንነበር? ☐ከሸሪዓጋርየማይጻረርአማራጭየፋይናንስአገልግሎትስለሌለ

☐ከሸሪዓጋርይጻረራሉብየስለማላምን

☐አገልግሎቱን መጠቀም ግደታ ስለሆነ

☐ሌላከሆነይግለጹ ____________________________________________

## III. <u>በኢትዮጵያመደበኛባንኮችስለሚሰጠዉከወለድነፃየባንክአገልግሎትያለዎትእወቅትናአጠቃቀም</u>

19. ከወለድነፃየፋይናንስአገልግሎቶች ምን እንደሆኑ

እናበኢትዮጵያመደበኛባንኮችከወለድነፃየባንክአገልግሎትእየተሰጠእንደሆነያዉቃሉን?

☐አላውቅም☐አዉቃለሁ

20. ከሚከተሉትከወለድነፃየባንክአገልግሎቶችመካከልየትኞቹን/የትኛዉንእየተጠቀሙይገኛሉ?

☐ዋዲያህ☐አማና

☐ሙዳረባህ☐ሙራበሃ

☐ሌላከሆነይግለጹ ____________________________________________ ☐አልጠቀምም

21. ለጥያቄቁጥር 21 መልስዎአልጠቀምምከሆነምክንያትዎምንድን ነው?

☐አገልግሎቱበመደበኛባንክበመስጠቱ

☐ከመደበኛባንክአገልግሎቶችየተለዩናችዉብዬስለማላምን

☐ሞክሬስላልተሳካልኝ

☐ሌላከሆነይግለጹ ____________________________________________

## IV. <u>በኢትዮጵያሙሉየሆነከወለድነፃየፋይናንስአገልግሎትቢጀመር</u>

22. ሙሉየሆነከወለድ ነፃየፋይናንስበኢትዮጵያቢጀመርእርስዎበምንመልኩተሳታፊሊሆኑይችላሉ?

☐የአገልግሎቱተጠቃሚበመሆን ☐አክሲዮንበመግዛት

☐በማስተዋወቅ

23. በንግድላይተስማርተዉይገኛሉን?

☐አይ አልተሰማራሁም

☐አዎ(በምንአይነትንግድላይእነደተስማሩናለንግድዎየሚያስፈለግዎትንገንዘብከየትእንደሚያገኙያብራሩ) _

______________________________________________________________________

24. ንግድዎትንሲጀመሩከባንክወይምከማንኛዉምየፋይንንስተቋምገንዘብተበድረዉነበርን?

☐አልተበደርኩም

☐ተበድሪያለሁ (ምንአይነትብድርአንደሆነናከየትኛዉየፋይናነስተቋምአንደሆነ ያብራሩ) ______________

______________________________________________

______________________________________________

25. ለንግድዎየሚሆንገንዘብለማግኘትከወለድነፃየባንክአገልግሎትየሚሰጡባንኮችንጠይቀዉያዉቃሉን?

☐አልጠየቅኩም

☐ጠይቂያለሁ (ዉጤቱምንእነደነበርያብራሩ) ______________________________

______________________________________________

26. በርስዎአመለካከትምቹየሆነከወለድ
ነፃየፋይናንስአገልግሎትበኢትዮጵያቢጀመርበእርሰዎየንግድስትራቴጂላይሊፍጥረውየሚችለዉንተጽኖያብራሩ

______________________________________________

______________________________________________

| V. | በሀይማኖትምክንያትከፋይናንስአገልግሎቶችተጠቃሚስላለመሆንእናስለወለድነፃየባንክአገልግሎቶችያለዎትአመለካከት | | | | | |
|---|---|---|---|---|---|---|
| | | 1 | 2 | 3 | 4 | 5 |
| | | በጣምአልስማማም | አልስማማም | ገለልተኛ | እስማማለሁ | በጣምእስማማለሁ |
| 27 | የኢትዮጲያፋይናንስበወለድላይመሰረትያደረገስለሆነሙስሊሞችተጠቃሚእየሆኑአይደለም | | | | | |
| 38 | በኢትዮጲያሙሉየሆነከወለድነፃፋይናንስቢጀመርፋይናንስንለሁሉምህብረተሰብተደራሽለማድረግ፣ድህነትንለመቀነስአናኢኮኖሚንለማሳደግትልቅፋይዳይኖረዋል | | | | | |
| 29 | ኢትዮጵያዊያንሙስሊሞችየተሟላከወለድነፃየፋይናንስአገልግሎትቢያገኙማህበራዊእናኢኮኖሚያዊችግሮቻቸዉሊቀረፍይችላል፤የንብረትባለቤትሊሆኑይችላሉ፣በኢንቨስትመንትሊሳተፉይችላሉ. | | | | | |
| 30 | በታሪክእንደሚታወቀዉኢትዮጵያዉያንሙስሊሞችበንግድናየተለያዩሞያዎችላይተሰማርተዉሀገራቸዉንሲያገለግሉኖረዋል ።<br>ነገርግንበአሁኑጊዜሙስሊሞችሸሪዓዉንመሰረትያደረገየፋይናንስምንጭባለማግኘታቸዉከነዚህሴክተሮችተገለዋል | | | | | |
| 31 | ከወለድነፃየባንክአገልግሎቶችበመደበኛባንኮችቢሰጡምሙስሊሞችአገልግሎቶቹንእንዲጠቀሙአያበረታታም | | | | | |
| 32 | በኢትዮጵያሙሉየሆነእስላማዊየፋይናንስአገልግሎትቢጀመርእሱንመጠቀምእመርጣለሁ | | | | | |

**Appendix G: Tez Fotokopisi İzin Formu**

**ENSTİTÜ**

Fen Bilimleri Enstitüsü ☐

Sosyal Bilimler Enstitüsü ☐

**YAZARIN**

Soyadı: Haılu
Adı: Suadiq
Bölümü: Bankacılık ve Finans

**TEZİN ADI**(İngilizce): THE ROLE OF ISLAMIC FINANCE IN REDUCTION OF FINANCIAL EXCLUSION IN ETHIOPIA

**TEZİN TÜRÜ**: Yüksek Lisans ☐ Doktora ☐

1. Tezimin tamamından kaynak gösterilmek şartıyla fotokopi alınabilir. ☐

2. Tezimin içindekiler sayfası, özet, indeks sayfalarından ve/veya bir bölümünden kaynak gösterilmek şartıyla fotokopi alınabilir. ☐

3. Tezimden bir (1) yıl süreyle fotokopi alınamaz. ☐

**TEZİN KÜTÜPHANEYE TESLİM TARİHİ**