

Do Islamic Microfinance Products Enhance the Microenterprise's Development in Mauritania?

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Received: September 20, 2022

Last Revised: October 22, 2022

Accepted: November 22, 2022

Abstract

This study investigates the impact of using Islamic microfinance products on the microenterprise's development in Nouakchott-Mauritania and tests the moderator effect of gender. The data is collected from 381 beneficiaries of PROCAPEC-Nouakchott through a questionnaire. Structural equation modeling is utilized to test the hypothesis. The results show that the usage of Islamic microfinance products has a positive impact on microenterprises. Nonetheless, gender has no moderator effect in the model. Based on these findings, policymakers and managers of Islamic microfinance institutions are highly recommended to ease the usage of Islamic microfinance products for micro-entrepreneurs to increase their productivity and financial independence.

Keywords: Mauritania, Islamic Microfinance, Financial Inclusion, Microenterprises Poverty Alleviation, Structural Equation Modeling.

1. Introduction

Expanding financial access and usage to microenterprises is still a major challenge for several governments in the developing countries. The World Bank (2018) projects in its latest estimate that by 2030 the poverty in Sub-Saharan African countries will be around 90 per cent. This fact threatens Mauritania because its economy is fragile and vulnerable with real GDP growth of only 3.5 per cent in 2017 and a low exportation rate. Therefore, this research investigates an alternative strategy to alleviate poverty and reduce financial exclusion in Mauritania. Since the Islamic Republic of Mauritania is 100 per cent Muslim, the Islamic microfinance model can eradicate poverty and improve financial inclusion especially in the capital city Nouakchott. In Mauritania, the issue of poverty is alarming. Around 31 percent of the population lives in

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relative poverty, whilst 16.6 percent of people live in absolute poverty (ECA, 2016). The World Bank (2018) indicated that real annual growth in terms of household expenditure per capita was only 1.52 percent in 2014; the inequality (measured by the Gini index) was 31.9 in 2014. Only 38 per cent of people used electricity, 45 per cent of children were not enrolled in school, and one-third of households lived in precarious housing.

Apart from that, financial exclusion is also a pertinent problem in Mauritania which is at around 80 per cent (World Bank, 2015). In other words, only 20 percent of Mauritians have access to essential financial services. This fact can be caused by several reasons such as poverty, illiteracy, and youth unemployment leading to the exclusion of almost a quarter of the population in urban areas (ECA, 2016), and the situation is even worse in the rural areas. A study conducted by Amendola, Boccia, Mele, and Sensini (2016) revealed that most Mauritanian citizens deal and work in the informal sector “grey market,” which is neither controlled nor regulated by the government. As a result, the economic situation is worsened by the large informal sector that undermines the formal financial sector's growth affecting the whole country (ECA, 2016). Furthermore, the Net Enrolment Ratio (NER) of schools declined to 54.9 per cent in 2014. The unemployment rate was around 12.85 per cent in 2014, and the health coverage was limited to approximately 10 percent of the population. Also, the health index was just 68.8 per cent in 2018 (UNDP, 2018). The Human Development Index (HDI) was 0.506 which is a very low HDI as compared to other countries in the region thus ranking 156th globally. Besides this, the literacy rate is 45.5 per cent which is a low rate while comparing to other African countries.

Mauritians are willing to use Islamic finance more than the conventional tools due to religiosity barriers (Abduh & Mahmoud, 2014). This study was conducted in Nouakchott and showed that awareness positively affects the attitude and intention to use Islamic finance. Lately, Mauritania's central bank has conducted a workshop to facilitate the implementation of Islamic financial standards board (IFSB) norms in the country (CBM, 2019). Hence, there is a bright future for Islamic finance in the country. The Mauritanian government has implemented several policies to enhance the microfinance industry due to its importance in developing microenterprises. However, these policies did not fulfill the expectations and the microenterprises sector is still underdeveloped. The national strategy of microfinance has been adopted since 2003 by the Mauritanian central bank to develop both the sectors i.e., microfinance industry and microenterprises. For many years, the latter has been the government's

focus due to its high impact on the country's economy. Due to the Mauritanian government's efforts and policies, the sectors of microfinance and microenterprises are on an escalating trend (Bouasria, Ashta, & Ratsimalahelo, 2020).

Due to the high impact of microenterprises on the country's economic development, this study investigates the role of using Islamic microfinance for microenterprises development in Mauritania through the beneficiaries of the largest microfinance institution (PROCAPEC). Since the available studies are scarce on this topic in Mauritania, this study will be a milestone for researchers especially in the geographical context. The findings of this research will enrich literature and the body of knowledge related to microenterprises and Islamic microfinance.

This research paper comprises five sections and is organized as follows: the first section presents the introduction which includes the background of the topic, the research gap, and the objective of the study. The second section includes the literature review which contains a survey of the empirical and conceptual studies found on the topic and the theory underpinning the study.. The third section discusses data and methodology. The fourth section shows the results and analysis. Finally, the fifth section presents the conclusions, recommendations, and opens areas for future studies.

2. Literature Review

2.1 Supply-Leading Finance Theory

According to Robinson (2001), there are four theories related to microfinance: supply-leading theory, imperfect information theory, informal credit market theory, and saving of the poor theory. All these theories are related to some parts of this study. This study focuses on only one of these theories which is the supply-leading theory.

The supply-leading theory is based on giving loans before getting demand for credits to boost the economy's investment. This theory has been found to solve the severe poverty problem that emerged after World War II when governments encouraged banks to provide microcredits to competent people especially farmers to improve the agriculture sector and make investments to elevate the well-being of people and societies (Randhawa, 2004). This theory explains that finance is an effective way to boost economic growth. However, some researchers found that the Following Demand Theory is more effective in some specific contexts than in others (Adeyeye, Fapetu, Aluko, & Migiro, 2015). The Following Demand Theory states that financing is provided only when

desired by the customers to use it. This theory is the inverse of the supply leading theory. The latter is relevant to this study because it links the usage of financial products with investment (microenterprises) which is a mediator in this research model.

Modern development theory emphasizes that financial exclusion is the main barrier to developing microenterprises and the economy in general (Beck, Demirgüç-Kunt, & Honohan, 2009). Financial market imperfections such as asymmetry of information can lead to the exclusion of microenterprises from the financial system. A developed economy is in contradiction with income inequality; therefore, providing opportunities to economically active individuals to raise their financial dependence by generating sustainable income. Financial inclusion is the solution to reduce income inequality and poverty. Consequently, a high economic growth rate is achieved. Lack of using financial products is the consequence of microenterprises underdevelopment due to their limited collateral, connections, and own resources (Beck et al., 2009; Beck, Demirguc-kunt, Soledad, & Peria, 2006).

2.1 Previous Studies

There are two types of microenterprises: growth enterprises and livelihood enterprises (Obaidullah, 2008b). The former is the main source of the entrepreneur and oriented for the development in the long term; whereas, the latter is directed by very poor people and is oriented just to be sustained to

survive the entrepreneurs. According to Obaidullah (2008), Islamic microfinance has several products: micro-Murabaha, qard hassan, micro-equity, micro-saving, micro-takaful, and micro-transfers. These products can enormously help low-income people in getting financially included. People who are financially excluded are mostly excluded from the economic development of their countries. Accessing Islamic banks is not a suitable choice for the vulnerable due to the high cost of products. Therefore, Islamic microfinance can be a solution to offer access and usage of financial products for micro-entrepreneurs who do not have financial access otherwise.

Microfinance institutions are mostly focused on micro-entrepreneurs to enhance the profitability of their business by offering affordable financial products and financial literacy training. Indeed, the financing to non-entrepreneurs or economically non-active people may increase their poverty level and bind them in a vicious circle because they will not repay the financing obtained from the institutions. It will be just for consumption. In Ghana, beneficiaries of microfinance have improved their socio-economic status by

using financial products offered (Dzisi & Obeng, 2013). There is a positive impact of using microfinance products on microenterprises performance (Rathirane & Semasinghe, 2016).

Microfinance Institutions (MFIs) are financial institutions that provide small credits and loans, insurance, and saving services to the people who do not have access to other financial services and products (Mukherjee, 1998). Yunus (1998) indicated that microfinance is a method to alleviate poverty due to its ability to provide funds to the productive population excluded from the financial system to generate income and help businesses flourish. Islamic microfinance can be compelling to the Mauritanian population due to its convenient features that aim to assist the poor first.

Additionally, the role of microfinance in poverty alleviation has been explained in many studies such as Abdul-Majeed Alaro & Alalubosa, (2018); Abdul Rahman & Dean, (2013); Khaki & Sangmi, (2017). They stated the potential of reducing the number of poor by using microfinance products and services. The impact of microfinance on people's lives, especially women's lives, has been proven by various studies (Hassan & Saleem, 2017; Murshid, 2018). Further, a study conducted by Kasali, Ahmad, and Ean (2015) found that microfinance institutions loans significantly decreased the customers' vulnerability. Even though microfinance is useful for uplifting vulnerable people's conditions, many poor are still excluded due to the fear of non-repayment, particularly the women (Ukanwa, Xiong, & Anderson, 2018). Other factors can also negatively affect microfinance institutions' access, such as illiteracy and lack of necessary financial infrastructures (Ali, 2017).

Islamic microfinance improves its customers' socio-economic situation (Ahmad, Adewale, & Khan, 2017). Numerous studies have shown that Islamic microfinance assists in poverty alleviation in most Muslim countries such as Indonesia, Malaysia, Bangladesh, and Pakistan. For instance, Rokhman (2013) has studied Islamic microfinance's role in poverty alleviation in Indonesia. In the study, poverty was measured by four dimensions including income level, children's education, business program, and health care. The research found that Islamic microfinance has a significant positive impact on three dimensions of poverty: income level, children education, and business progress. However, there was no impact of Islamic microfinance on health.

Moreover, Mahmood, Fatima, Khan, and Qamar (2015) examined the role of Islamic microfinance (IsMF) on Pakistan's poverty alleviation and found that IsMF improved the poor's lives in several domains. Interestingly, financing micro-enterprises is more efficient than financing a group of impoverished individuals. Islamic microcredit has been found to improve women's well-being

by expanding their small businesses (Rashid & Ejaz, 2019). Islamic microfinance promotes good saving habits among its customers by imposing rules such as saving before borrowing schemes.

The role of financial development on poverty reduction has been proved by several studies (Rashid & Intartaglia, 2017), and access to finance has been shown to enhance the wellbeing and standards of living (Khaki & Sangmi, 2017). In Sub Saharan Africa (SSA), there is a mixed impact of micro saving and microcredit on poverty reduction. Rooyen, Stewart, and de Wet (2012) found that microfinance can, in some cases, enhance poverty by disempowering women. However, in other contexts, microfinance can increase poverty by forcing the poor to borrow from other channels to repay the financial institutions' loans.

Entrepreneurship means starting or reestablishing a business for making a profit by efficiently utilizing the economic resources that the entrepreneur has (Hussain, Bhuiyan, & Bakar, 2014). The development of entrepreneurship is a crucial factor to eliminate poverty by generating an income that makes an individual financially self-independent. Apart from the economic benefit, entrepreneurship has a social impact on individuals by giving them a sense of possession and self-confidence. According to Ahmed (2002), small and medium enterprises have a fixed number of workers and/or a fixed capital. The SMEs can be different based on their economic situation or the owner's financial status or qualification. Less fortunate people mostly own income-generating activities (IGAs) to make a living and be financially independent. Islamic microfinance increases the poor's income by financing their microenterprises which are their primary revenue source (Asmawati & Ahmad, 2015). Additionally, there is a positive impact of using microfinance products on the performance of microenterprises (Alkhan & Hassan, 2020; Rathirane & Semasinghe, 2016).

Shaikh (2017) suggested that Mudharaba is an ideal method to finance the medium and small microenterprises (MSEs) and boost the economy of less fortunate people ultimately leading to poverty alleviation. However, Mudharaba was not proven to be useful for microenterprises. Financing the microenterprises is one of the main objectives of IsMFIs through which less fortunate populations can enhance their financial position (Ahmed, 2002; Obaidullah, 2008a). Using Islamic microfinance products is vital for those with only one microenterprise, which is their livelihood business, to enhance its performance and sustainability. The usage of financial products can make the poor more productive in earning their livelihood and income-generating

activities (Asmawati & Ahmad, 2015; Tadesse & Zewdie, 2019). Islamic microfinance could help low-income entrepreneurs to create income generation and enhance their living standards (Adnan & Ajija, 2015; Mosaddak Ahmed Chowdhury, Rahman, & Salman, 2021)

Islamic microfinance has numerous benefits not only on poverty alleviation but also on women empowerment, financial inclusion, and financial stability. Access to microfinance enables women to control their resources (Murshid, 2018) and improve their assets (Ukanwa, Xiong, Anderson, et al., 2018). The usage of financing offered by Islamic microfinance institutions improved the micro-entrepreneur's assets owned, living standards, education level, ethical values, profitability, and sustainability (Aslam, 2014; Bhuiyan, Siwar, Ismail, & Omar, 2017c; Mohamed & Fauziyyah, 2020).

According to Bhuiyan and Siwar (2017), microfinance leads to income-generating activities, thereby reducing poverty among microfinance customers. This is due to the excellent investment of finance taken from microfinance institutions and the monitoring of the business process by microfinance operators. Microenterprises can be improved by Islamic equity-financing modes which enable the reduction of agency-risks so that they can sustain the and elevate the economic situation of low-income people (Adnan & Ajija, 2015; Shaikh, 2017). Nonetheless, Fianto, Gan, Hu, and Roudaki (2017) stipulated that the best financing method is debt-based contracts for Islamic microfinance institutions because it is more effective than equity-financing. In other words, the study confirms that clients benefit more from Murabaha contracts than Mudharaba and Musharaka contracts.

A study conducted by Mahmood, Hussain, and Matlay (2014) has investigated the effect of microfinance loan size on the development of microenterprises owned by women. The study discussed that microfinance institutions significantly affect income-producing activities through peer monitoring strategies, advice, training opportunities, and regular meetings. MFIs improve women's financial independence, empowerment, and business skills. The findings also revealed that the larger the loan taken, the lower the income generated; thus, women should take only small-sized loans to gain more profits. Previous studies have shown the positive role of Islamic microfinance in encouraging and developing businesses and microenterprises (Nobi, Billah, & Shohel, 2021; Rokhman, 2013).

On the other hand, conventional microfinance enhances SMEs' growth; for instance, Self Help Group (SHG) has played an essential role in alleviating some of the Indian's poverty by financing a small business. A study conducted by Sivachithappa (2013) on 186 women in India revealed that SHG had empowered women by using loans in income-generating activities. Further, the results found that women became more independent in decision-making due to the increased income and assets. Also, Amanah Ikhtiar Malaysia (AIM), as a microcredit organization, has helped numerous Malaysian women to increase their income by financing small businesses and microenterprises (Samer et al., 2015). In Ghana, the beneficiaries of microfinance have improved their socio-economic status by using financial products offered (Dzisi & Obeng, 2013). A similar impact can be obtained in Mauritania due to the similarity in economic conditions of both the countries.

Nevertheless, some studies showed that Microfinance did not encourage low-income micro-entrepreneurs to grow their business which addressed only ultra-poor micro-entrepreneurs (Abbas & Shirazi, 2015). There are mixed findings on microfinance effects on microenterprise development which have been discussed by several studies (Sani & Mohd-khan, 2016). In other words, microfinance has positively affected the development of SMEs in some countries but does not participate in the development of others in different contexts. A study from Indonesia found that microfinance products usage may not affect microenterprise development (Atmadja et al., 2018). Hence, the following hypotheses are elaborated:

H1. Usage of Islamic microfinance products has a positive impact on the development of the microenterprise in Nouakchott-Mauritania.

H2. Gender moderates the relationship between the use of Islamic microfinance products and microenterprises development in Nouakchott-Mauritania.

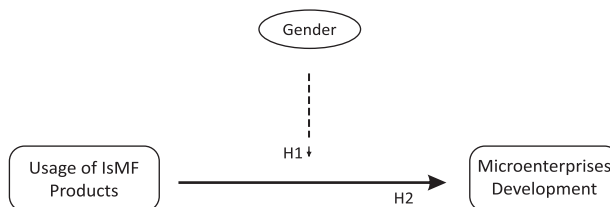


Figure 2.1. Conceptual Framework

3. Data And Methodology

3.1 Data

The data for this study were collected through a questionnaire. Using a purposive sampling method through a cross-sectional design, 700 copies of the survey questionnaire were distributed to the beneficiaries of the Islamic microfinance PROCAPEC-Nouakchott out of which, 493 questionnaires were returned which indicates a response rate of 71 per cent. After data screening and deleting the outliers, the remaining usable data is 381. This response rate is acceptable because it is above the cut score of 50 per cent (Yun & Trumbo, 2000). Indeed, this response rate is also due to the limited experience of the Mauritians who are not familiar with the surveys and most of the respondents were unwilling to answer the questionnaire. After several visits by the researcher to the institutions, enough sample size was achieved.

3.2 Model Development

3.2.1 Measurement of the dependent variable

The dependent variable in this study is the development of the microenterprise managed by Mauritanian who are the beneficiaries of Islamic microfinance PROCAPEC located in Nouakchott. The items of the variables were adapted from different studies with some modifications. The variable has eight items, but three were deleted due to the factor loadings in the measurement model. The variable is measured using a five-Likert scale ranging from 1 (strongly disagree), 2(disagree), 3(neutral), 4(strongly agree), and 5 (strongly agree). The variable has a Cronbach alpha greater than 0.7 which indicates the strong reliability of the items.

3.2.2 Measurement of the independent variable

The independent variable of the study is the usage of Islamic microfinance products offered in PROCAPEC-Nouakchott. The variable is self-developed, and it is measured by a four-Likert scale ranging from 1(never used), 2(rarely used), 3(sometimes used), 4 (frequently used). The products here are four: Murabaha, Qard Hassan, Saving, and Remittance. The variable has a Cronbach alpha greater than 0.7 which indicates the high adequacy and reliability of the items.

Table 3.1: Reliability of Constructs

Variable	Number items	of Cronbach's Alpha
Usage	4	.790
MEnt-Dev	5	.921

4 Results and Analysis

4.1 Measurement Model

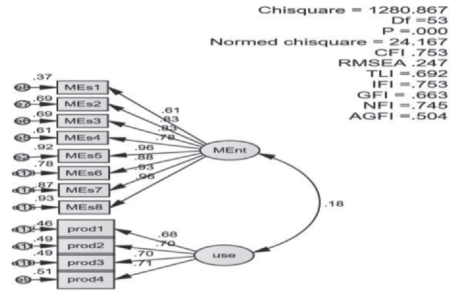


Figure 4.1 Measurement Model

From Figure2, it is found that the measurement model is not valid because the indices do not follow the rule of thumb. Therefore, some modifications are indispensable to fix the model.

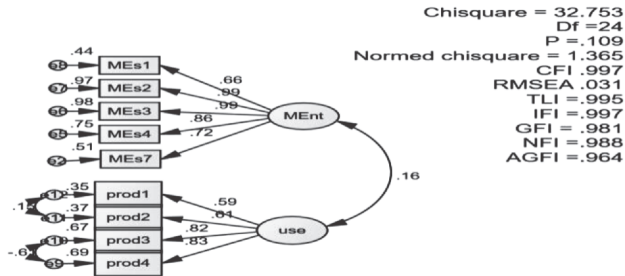


Figure 4.2 Modified Measurement Model

The model presented in Figure 4.2 is valid and the indices follow the rule of thumb. Therefore, the hypothesized model can be elaborated. The summary of all the indices is presented in Table 4.2.

Table 4.2: Summary of the Measurement Model Indices

Indices	Rule of thumb	Value in the model
Normed chi-square	<5	1.365
P-value	>0.005	.109
CFI	>.90	.997
RMSEA	<.08	.031
IFI	>.90	.997
TLI	>.90	.995
GFI	>.90	.981
NFI	>.90	.988
AGFI	>.90	.964

Table 4.3: Convergent and Discriminant Validity

	CR	AVE	MSV	MaxR(H)	Ment-Dev	Usage
Ment-Dev	0.930	0.731	0.025	0.990	0.855	
Usage	0.807	0.518	0.025	0.843	0.159	0.720

Based on the table above Table 4.3 there is no validity issue and the model is generally valid. The composite reliability for both the variables is greater than 0.7 which indicates strong adequacy of the items used.

4.2 Structural Equation Modeling

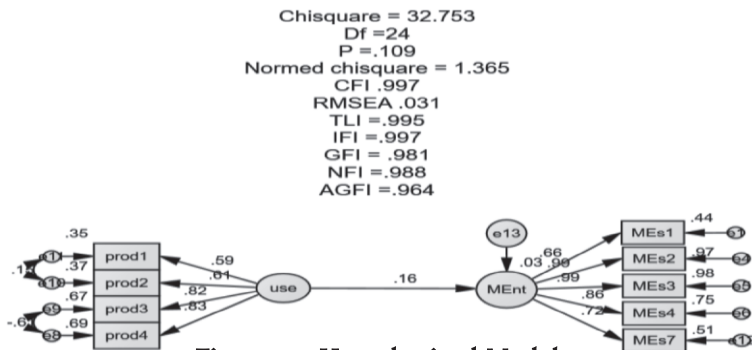


Figure 4.3 Hypothesized Model

Figure 4.3 shows that the model is valid and fit because all the indices are above the cut-score. For instance, the CFI >0.9; RMSEA<0.08; and Normed chi-square <5. Therefore, the second step of testing hypotheses can take place. Table 4.3 presents the hypothesis result.

Table 4.4: Regression Weights and Hypothesis decision

		Estimate	S.E.	C.R.	P	DECISION
Use →	MEnt	.240	.111	2.163	.031	H1 ACCEPTED

The relationship between the usage of Islamic microfinance products and microenterprises development is positive and statistically significant because $p=0.031<0.05$ and $C.R.=2.163>1.96$; therefore, the hypothesis (H1) is supported and accepted. This result is in line with several studies (Hassan & Islam, 2018; Rathiranee & Semasinghe, 2016; Shaikh Ismail, & Mohd Shafiai, 2017). These studies found that the usage of islamic microfinance improves the performance of microenterprises. This finding is also aligned with the supply-leading finance theory, explaining the strong relationship between microenterprises and

financial products usage. Most Mauritians are active and willing to work if they get access to financial aid; hence, Islamic microfinance is the best option for improving their business and small projects.

Moreover, Gender does not affect the relationship between Islamic microfinance and microenterprises development as shown in Table 4.5 The z-score is greater than 0.5, hence there is no gender invariance in the model. This result is in line with the findings of Atmadja et al., (2018) who found that gender is not an important factor in the relationship between Islamic microfinance and microenterprises development.

Table 4.5: Gender Moderation Effect

	Male		Female		z-score
	Estimate	P	Estimate	P	
Use→MEnt Development	0.134	0.495	0.299	0.018	0.708

5 Conclusions and Recommendations

The main objective of this study is to determine the impact of using Islamic microfinance products on microenterprise development and also to examine the gender invariance in the study. The hypothesis (H1) is significant and positive. Hence, Islamic microfinance products and services have enormously helped micro-entrepreneurs develop their business and small economic activities. Thus, Islamic microfinance was an indispensable tool for the low-income Mauritanian micro-entrepreneurs to develop and diversify their income-generating activities. This result is in line with several studies which stipulated that Islamic microfinance can improve microenterprises and enhance their sustainability (Bhuiyan, Siwar, Ismail, & Omar, 2017; Fianto et al., 2017; Murshid, 2018; Shaikh, 2017; Tadesse & Zewdie, 2019). Gender has no moderator effect on the relationship between the use of Islamic microfinance products and microenterprises in Mauritania. Therefore, H2 is rejected.

The entrepreneurship sector in Mauritania is fragile. Due to its enormous advantages on the country's economy, it is recommended that the Mauritanian government implement more strict regulations to preserve the Moreover, Gender does not affect the relationship between Islamic microfinance and microenterprises development as shown in Table 5. The z-score is greater than 0.5, hence there is no gender invariance in the model. This result is in line with the findings of Atmadja et al., (2018) who found that gender is not an important factor in the relationship between Islamic microfinance and microenterprises development.

entrepreneurship sector and reduce the taxes imposed on their businesses. Strategies that develop the private sector should be carried out to eradicate

poverty and build the country's economy. Micro-entrepreneurs are numerous in Mauritania, but they lack access to finance leading to business loss and bankruptcy. Since this study found that microenterprises can reduce poverty, it is endorsed that the government and Islamic institutions encourage and develop the private sector to achieve the financial independence and shared prosperity of the poor.

Microfinance institutions managers should be advised to adopt financial literacy training programs to educate customers to perform well in their businesses. The absence of supervision from the financial institutions leads to the collapse of several microenterprises. The managers and operators of Islamic microfinance institutions should enhance awareness of the products. Also, understanding the difference between access and usage of products is indispensable to maintain the clients. This is because having access to the services offered does not infer the effective usage of the services. A massive number of micro-entrepreneur clients does not use the products provided just because they are not aware of it. Therefore, recruiting knowledgeable and approachable officers is crucial to enhance marketing of the products and increase their usage. Additionally, reducing the stringent rules for documentation is vital for easing financial products usage by low-income and uneducated people. The more the products are affordable and services are diversified and well presented to the clients, the better the institution's outcome will be.

Micro-entrepreneurs are worthy of getting financing due to their ability to increase the country's economy. Therefore, Microfinance institutions should attract micro-entrepreneurs by adopting approaches such as opening free-accounts, KYC (know your customer) procedures, and other facilities regarding free financial advice. Boosting micro-entrepreneurs to be financially included can enhance the motivation among several Mauritians who become hopeless in getting finance to start their business activities and improve their socio-economic wellbeing.

Even though this study has a great value added to the body of knowledge in microfinance and poverty, it has some limitations too. Firstly, it is purely quantitative. Future studies can use qualitative methods to enrich the results of the study. Secondly, this research has focused only on one microfinance institution in Nouakchott. Other studies may include other microfinance institutions or different financial institutions such as takaful institutions or Islamic banks in the Mauritanian context.

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